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Note by the Secretary-General

The Secretary-General has the honour to transmit herewith to the Security Council the report of the Board of Auditors on the financial statements of the United Nations Escrow (Iraq) Account for the financial period year ended 31 December 2004.

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Report of the Board of Auditors on the accounts of the United Nations Escrow (Iraq) Account established under the provisions of Security Council resolutions 986 (1995), 706 (1991), 778 (1992), 687 (1991), 1284 (1999), and 1483 (2003) for the financial period ended 31 December 2004

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31 March 2005

Dear Mr. Chairman,

In accordance with financial regulation 6.5, I have the honour to submit the accounts of the United Nations Escrow Account established pursuant to Security Council resolution 986 (1995), and pursuant to Security Council resolutions 687 (1991), 706 (1991), 778 (1992), 1284 (1999), 1483 (2003) and 1546 (2004), for the 12-month period of the biennium 2004–2005 ending 31 December 2004, which I hereby approve. The financial statements have been completed and certified by the Acting Controller.

(Signed) Kofi A. **Annan**

Mr. Guillermo N. Carague
Chairman
United Nations Board of Auditors
New York

06-42677

I. Report of the Board of Auditors

Executive summary

The Board of Auditors has audited the operations of the United Nations Escrow (Iraq) Account established under the provisions of Security Council resolutions relating to Iraq for the financial period ended 31 December 2004.

The Board issued an unqualified opinion on the financial statements for the United Nations Escrow (Iraq) Account for the financial period ended 31 December 2004, as reflected in chapter II.

Implementation of previous recommendations

The Board has indicated in the annex to the present chapter, the summary status of implementation of recommendations for the period 1 January to 31 December 2003. The two recommendations were under implementation.

Financial overview for the financial period ended 31 December 2004

Shortfall of income over expenditure for the period registered at $245.68 million, after deducting the total expenditure and prior-period adjustments of $368.84 million from total income, comprising interest and miscellaneous, of $123.16 million. Total expenditure has decreased by $923.32 from $9.692 billion in 2003 to $368.84 million in 2004. Total assets posted a decrease of $15.28 million, from $18.84 million in 2003 to $3.56 million in 2004, which is attributable mainly to the continued settlement of unliquidated obligations and transfers to the Development Fund for Iraq.

The Board reviewed five major accounts in the financial statements, inter alia, (i) revenues; (ii) expenditures on humanitarian supplies and related expenses; (iii) assets, the bulk of which was in cash and investments; (iv) liabilities, which are essentially unliquidated obligations for approved/amended contracts; and (v) reserves and fund balances as at 31 December 2004. In line with this review, the Board noted the following:

(a) A total of 202 letters of credit amounting to $248.68 million, which expired on 1 October 2004 and earlier, were still included in the Banque Nationale de Paris (BNP) liability report;

(b) The balance of unliquidated obligations as at 31 December 2004 disclosed a difference of $35 million with the BNP Paribas liability report;

(c) Letters of credit amounting to $31.1 million, which expired in 2004 owing to failure of suppliers to deliver, were cancelled and the related adjustments in IMIS were posted only during January to March 2005;

(d) The currency amounts of obligations raised/closed in the financial period 2004 were translated, using exchange rates other than the 31 December 2004 rates;

(e) The shipment and validity dates of certain letters of credit were repeatedly extended since the contracts were amended under Security Council resolution 1483 (2003);

(f) The payable to the Government of Germany amounting to $0.58 million remained outstanding since 1992 owing to differing opinion/interpretation on whether Germany could be reimbursed under paragraph 8 (e) of Security Council resolution 986 (1995).

The Board made recommendations for the Administration to: (a) continue to coordinate closely with the Banque Nationale de Paris Paribas on the timely and practicable cancellation of letters of credit, which had expired, particularly in respect of those without valid claims; (b) continue to reconcile the balances of unliquidated obligations against the Banque Nationale de Paris Paribas liability report on a per obligation basis and reflect the adjustment in the financial period to which it relates, whenever practicable; (c) ensure that all transactions pertaining to a particular period are taken up during the same period; (d) coordinate with the IMIS team regarding the currency exchange rates that would be used in the translation of balances of obligations raised or closed as at cut-off date; (e) continue to review the obligations related to amended contracts and effect the adjustments in IMIS; (f) take steps, in conjunction with the United Nations Monitoring, Verification and Inspection Commission (UNMOVIC), to determine whether the payable to the Government of Germany represents a valid claim against the funds of the programme in order to clear the balance.

A list of the Board's main recommendations appears in paragraph 20 of the present report.

A. Introduction

1. The Board of Auditors has audited the financial statements of the United Nations Escrow (Iraq) Account established under the provisions of Security Council resolutions relating to Iraq, in accordance with Security Council resolutions 986 (1995), 1483 (2003) and 1546 (2004), and pursuant to Security Council resolutions 687 (1991), 706 (1991), 778 (1992) and 1284 (1999), and the memorandum of understanding signed in May 1996 between the Secretariat of the United Nations and the Government of Iraq. The audit was conducted in conformity with article VII of the Financial Regulations and Rules and the annex thereto, and the common auditing standards of the Panel of External Auditors of the United Nations, the specialized agencies and the International Atomic Energy Agency and the International Standards on Auditing. Those standards require that the Board plan and perform the audit to obtain reasonable assurance as to whether the financial statements are free of material misstatement. The report is addressed to the Secretary-General, who is invited to forward it to the President of the Security Council.

2. The audit was conducted primarily to enable the Board to form an opinion as to whether the expenditures and unliquidated obligations recorded in the financial statements for the financial period from 1 January to 31 December 2004 had been incurred for the purposes approved by the Committee established under Security Council resolution 661 (1990) and in pursuance of the provisions of Security Council resolution 1483 (2003), whether income and expenditures, cash and investments, advances and other receivable/payable accounts were properly classified and recorded in accordance with the Financial Regulations and Rules, and whether the financial statements of the United Nations Escrow (Iraq) Account established under the provisions of the Security Council resolutions relating to Iraq presented fairly the financial position as at 31 December 2004.

3. The audit included a general review of the financial systems and tests of the adequacy of the existing controls over cash investments and related income, payments of expenditures, advances to agencies and unliquidated obligations to obtain assurance that payments for expenditures were made for valid obligations, the recorded obligations represent valid claims and transfers of funds were made in pursuance of the provisions of resolution 1483 (2003). Likewise, the Board performed a test examination of accounting records and other supporting evidence, to the extent the Board considered necessary, to form an opinion on the financial statements.

1. Background

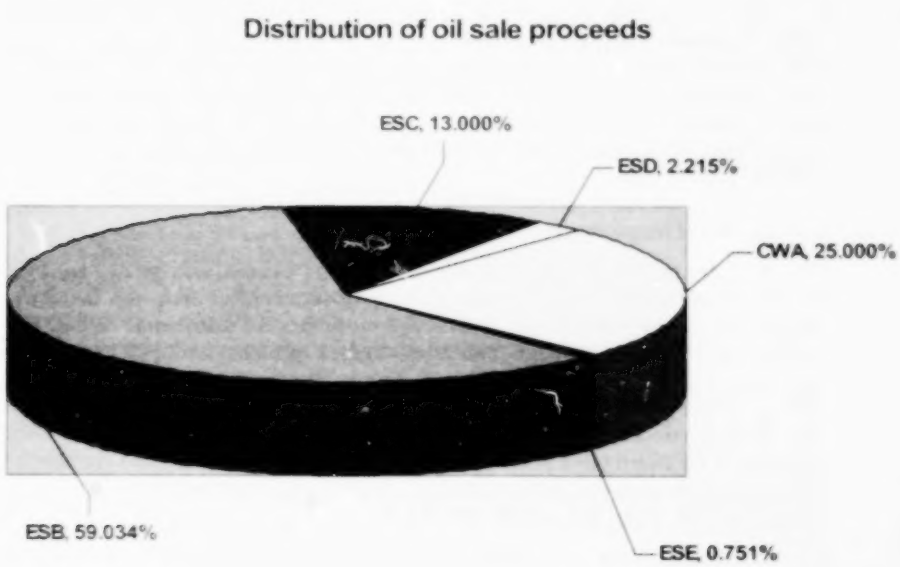
4. In August 1990, the Security Council adopted resolution 661 (1990) by which it imposed comprehensive sanctions on Iraq following that country's invasion of Kuwait. Concern over the humanitarian situation in Iraq, the United Nations proposed measures to enable Iraq to sell limited quantities of oil to meet its people's needs under resolutions 706 (1991) and 712 (1991) but were declined by the Government of Iraq.

5. In its resolution 986 (1995), the Security Council authorized Member States, for a period of 180 days, to permit the import of petroleum and petroleum products originating in Iraq sufficient to produce a sum not exceeding a total of $1 billion

every 90 days. The Oil-for-Food Programme began in December 1996 after the United Nations and the Government of Iraq agreed on the details of the implementation of resolution 986 (1995) through a memorandum of understanding of 20 May 1996. The funds thus generated through oil sales were to be credited to an escrow account, called the Iraq Account, established by the Secretary-General and used to meet the humanitarian needs of the Iraqi population as well as for other purposes specified in resolution 986 (1995), including financing of export of humanitarian supplies to Iraq particularly in the central and southern governorates (Fund ESB), complementing the distribution by the Government of Iraq of such supplies to the three northern Governorates of Arbil, Dihouk and Suleimaniyeh (Fund ESC), transferring the costs for the settlement of claims against damages and losses as a result of invasion and occupation of Kuwait by the Government of Iraq (Fund CWA), as well as for the monitoring, verification and inspection of weapons of mass destruction (Fund ESE) and meeting the programme's operational and administrative costs, including the cost of inspection agents (Fund ESD). The percentages of allocation are shown in the figure below.

Figure

Percentile distribution of the proceeds of oil sales pursuant to Security Council resolution 1330 (2000)



6. The Security Council in its resolution 986 (1995) also permitted the sale of additional quantities of oil by Iraq. It was envisaged that the revenue generated should be sufficient, after crediting 30 per cent thereof to the United Nations Compensation Commission (Fund CWA), to defray the cost of transportation of oil through the Kirkuk-Yumurtalik pipeline across the border between Iraq and Turkey (for shipment from the port of Ceyhan in Turkey) and accounted for in a separate fund, Fund ESF. As at 31 December 2003, Fund ESF had zero balance after settlement of the last invoice for the pipeline charges in June 2003. By virtue of Security Council resolution 1330 (2000), the share of the United Nations Compensation Commission was reduced to 25 per cent. Further, as provided under paragraph 21 of Security Council resolution 1483 (2003), 5 per cent of the proceeds of all sales of petroleum, petroleum products and natural gas from Iraq following the date of the adoption of the resolution would be deposited into the Compensation Fund.

7. In June 1998, under Security Council resolution 1153 (1998), the level of oil exports under the programme was raised to $5.26 billion for every six months. By virtue of Security Council resolution 1284 (1999), the ceiling of Iraqi oil exports was completely removed by the Security Council.

8. Owing to the outbreak of war in Iraq on 19 March 2003, the last oil shipment under the programme was made on 20 March 2003.

9. That situation in Iraq and the then ongoing investigation by the Independent Inquiry Committee on the United Nations Escrow (Iraq) Account contributed to the delay in the preparation of the present report as the Board's audit was rescheduled from sometime in March-April 2005 to May-June 2005. Pending the publication of the last report by the Independent Inquiry Committee, the Board has issued the management letter dated 7 June 2005 to the Controller covering the results of the audit for 2004.

2. Distribution of humanitarian supplies

10. Pursuant to the memorandum of understanding entered into on 20 May 1996 by and between the United Nations and the Government of Iraq, the latter was responsible for the procurement of food and medicines for distribution to the three northern governorates through concerned United Nations entities. The United Nations Office of the Iraq Programme, acting in coordination with the United Nations Office of the Humanitarian Coordinator in Iraq as its field office, was the focal point for tracking and coordinating all activities regarding the preparation and approval of the distribution plan; evaluation, processing, circulation and approval of contract applications; authentication of the delivery of goods and quality checks by the independent inspection agents; and distribution of supplies.

11. The programme was extended for 180 days from 5 December to 3 June 2003 by Security Council resolution 1447 (2002). The Council further adopted resolution 1472 (2003) to effect, on an interim and exceptional basis, technical and temporary adjustments to the Oil-for-Food Programme, and granted the Secretary-General authority for a period of 45 days to undertake measures to facilitate the delivery of humanitarian supplies and equipment. By its resolution 1476 (2003), the Security Council decided that the provisions contained in paragraph 4 of resolution 1472 (2003) would remain in force until 3 June 2003. On 22 May 2003, by resolution 1483 (2003), the Security Council lifted the civilian sanctions against Iraq. In the

same resolution, the Council ordered the termination of the Oil-for-Food Programme on 21 November 2003 and authorized the transfer of responsibility for the administration of its remaining activities to the Coalition Provisional Authority in Iraq.

3. Prioritization of contracts pursuant to Security Council resolution 1483 (2003)

12. In accordance with paragraph 16 of resolution 1483 (2003), the now-defunct United Nations Office of the Iraq Programme, in coordination with the Coalition Provisional Authority in Iraq and the relevant Iraqi authorities reviewed the relative utility of each contract still in the pipeline, and in exceptional cases included also those unfunded contracts. As at 21 November 2003, the United Nations Office of the Iraq Programme confirmed 3,060 contracts valued at about $6.210 billion as shown in table 1. The validity of the letters of credit issued and outstanding was extended or new letters of credit issued subject to the amended agreements between/among the suppliers, participating United Nations funds and programmes, and specialized agencies. The expiry dates of the letters of credit extend up to 2007.

Table 1
Results of prioritization of contracts pursuant to Security Council resolution 1483 (2003)

Category	*Number of contracts*	*Value (billions of United States dollars)*
Approved and funded contracts prioritized and amended by the United Nations	2 394	5.004
Previously non-funded contracts prioritized and amended by the United Nations	415	0.794
Approved and funded contracts that could not be amended by the United Nations by the deadline of 21 November 2003 and transferred "alive" to the Coalition Provisional Authority in Iraq for further processing	251	0.412
Total	**3 060**	**6.210**

13. The prioritization exercise also placed into separate categories some 728 previously approved and funded contracts that were prioritized but subsequently removed from the list of contracts amendable by the participating United Nations entities; 762 approved and funded contracts but not prioritized (contracts with "questionable utility"); and 709 approved and funded contracts with relatively small outstanding deliverables and regarding which suppliers appeared not interested in fulfilling its contractual obligation. The validity of the covering letters of credit of these contracts would be allowed to expire but the decision to terminate the contracts would be held in abeyance until after an internationally recognized representative from the Government of Iraq would make its own determination as to the necessity of enforcing such contracts. The Treasury informed the Board that it had no knowledge of the action taken by the Government of Iraq on the non-prioritized contracts as the Government of Iraq representative did not communicate the status to the Security Council.

4. Oil sales

14. Iraq sold some 3,427 million barrels of oil to 248 companies from 1996 to 2003, aggregating $64.2 billion and covering 13 phases (table 2). Buyer-companies were selected and contracted directly by the Iraqi State Oil Marketing Organization. Contracts entered into by and between the Iraqi State Oil Marketing Organization and the buyers were the subject of review by the oil overseers duly appointed by the Secretary-General focusing on the pricing mechanism.

Table 2
Total oil sales

Phase	*Volume of oil (million of barrels)*	*Value of oil exported (millions of United States dollars)*
I	120.0	2 150
II	127.0	2 125
III	182.0	2 085
IV	308.0	3 027
V	360.8	3 947
VI	389.6	7 402
VII	343.4	8 302
VIII	375.7	9 564
IX	293.0	5 638
X	300.2	5 350
XI	225.9	4 589
XII	232.7	5 639
XIII	169.6	4 413
Total	**3 427.9**	**64 231**

5. Expenditures for humanitarian supplies and oil spares

15. The programme was expanded by the Security Council beyond its initial emphasis on food and medicines to include infrastructure rehabilitation and other sectors. Cumulative expenditures on humanitarian supplies and oil spares covering 13 phases reached $43.84 billion as at 31 December 2004 (see table 3).

Table 3
Expenditures for humanitarian supplies and oil spares
(Millions of United States dollars)

Biennium	*Humanitarian supplies*	*Oil spares*	*Total*
1996-1997	2 402	—	2 402
1998-1999	6 026	345	6 371
2000-2001	19 989	2 369	22 358

Biennium	*Humanitarian supplies*	*Oil spares*	*Total*
2002-2003	11 120	1 286	12 406
2004-2005 (ended 31 December 2004)	219	83	302
Total	**39 756**	**4 083**	**43 839**

6. Monitoring of weapons of mass destruction

16. The United Nations Monitoring, Verification and Inspection Commission (UNMOVIC) was established by the Security Council in its resolution 1284 (1999) to undertake the responsibilities with regard to, inter alia, verification of compliance by Iraq on resolutions pertaining to weapons of mass destruction. In view of the termination of the Oil-for-Food Programme, the Security Council in its resolution 1483 (2003) underlined its intention to revisit the mandates of UNMOVIC. Such intention was reaffirmed in its resolution 1546 (2004).

17. The present report covers matters that, in the opinion of the Board, should be brought to the attention of the Secretary-General and the Security Council. The Board discussed its observations and conclusions with the Administration, whose views, where appropriate, have been reflected in the report.

18. The Board's recommendations are reported in paragraph 20. The detailed findings are discussed in paragraphs 24 to 70.

7. Previous recommendations not fully implemented

19. The Board reviewed the measures taken by the Administration to implement the recommendations made in its previous reports. The two recommendations contained in the report of the Board of Auditors on the audit of the Escrow (Iraq) Accounts for the period ended 31 December 2003 were under implementation. Details of the action taken and the comments of the Board are included in the relevant discussion within the present report.

8. Main recommendations

20. The Board's main recommendations are that the Administration:

(a) **Continue to closely coordinate with BNP Paribas on the timely and practicable cancellation of letters of credit, which had expired, particularly in respect of those without valid claims (para. 33);**

(b) **Continue to reconcile the balances of unliquidated obligations against the BNP Paribas liability report on a per-obligation basis and reflect the adjustment in the financial period to which it relates (para. 40);**

(c) **Ensure that all transactions pertaining to a particular period are accurately recorded during the same period (para. 47);**

(d) **Coordinate with the IMIS Team regarding the currency exchange rates that would be used in the conversion of balances of obligations raised or closed as at financial statement date (para. 52);**

(e) **Continue to review the obligations related to amended contracts and effect the adjustments in IMIS in a timely manner (para. 56);**

(f) **Resolve, in conjunction with UNMOVIC, whether the payable to the Government of Germany still represents a valid claim against the funds of the programme in order to clear the balance (para. 60).**

B. Financial issues

1. Financial profile

21. The Board, as part of the financial review, analysed five major accounts of the financial statements: revenues; expenditures on humanitarian supplies and related expenses; assets, the bulk of which was in cash and investments; liabilities which are essentially unliquidated obligations for approved/amended contracts; and reserves and fund balances as at 31 December 2004.

22. Compared with the immediately preceding year, total income, the bulk of which came from oil sales, decreased by 53 per cent in 2003 and 97 per cent in 2004 owing to the interruption of oil sales on 20 March 2003. In 2004, interest income comprised 93 per cent of the total income amounting to $123 million. Expenditures for the humanitarian supplies and oil spares were $9.24 billion in 2002, $3.17 billion in 2003, and $302 million in 2004, or a decrease of $6.07 billion, and $2.87 billion in 2003 and 2004, respectively, owing to the termination of the programme in November 2003.

Table 4
Decreases in account balances
(Millions of United States dollars)

				Decrease in 2004		*Decrease in 2003*	
Account	*2004*	*2003*	*2002*	*Amount*	*%*	*Amount*	*%*
Total income	123	4 295	9 154	4 172	97	4 859	53
Total expenditures	369	3 471	9 692	3 102	89	6 221	64
Sale of Iraqi oil	—	3 308	10 240	3 308	100	6 932	68
Interest income	114	396	603	282	71	207	34
Purchase of humanitarian supplies and oil spares	302	3 168	9 238	2 866	90	6 070	66

23. As at 31 December 2004, cash and investments amounted to $3.54 billion. These adequately covered about $2.89 billion of unliquidated obligations arising from approved contracts for current and prior financial periods. The total reserves and fund balances decreased by $4.89 billion (88 per cent) from $5.55 billion in 2002 to $0.66 billion in 2004. The decrease resulted from fund transfers from 28 May 2003 to 31 December 2004 to the Development Fund for Iraq, as shown in table 5.

Table 5

Schedule of fund transfers to the Development Fund for Iraq from 28 May 2003 to 31 December 2004

(Billions of United States dollars)

Year	*Fund source*	*Date of transfer*	*Amount*	*Total*
2003	ESC	28 May 2003	1.000	
		31 October 2003	1.000	
		18 November 2003	1.000	
	ESB	31 December 2003	2.600	
Subtotal for 2003				**5.600**
2004	ESC	31 March 2004	0.696	
	ESB	31 March 2004	1.304	
		19 April 2004	0.400	
	ESD	19 April 2004	0.100	
	ESB	30 June 2004	0.500	
		3 November 2004	0.328	
	ESD	3 November 2004	0.100	
	ESB	30 December 2004	0.200	
Subtotal for 2004				**3.628**
Grand total				**9.228**

2. Winding-up process

24. After the termination of the Oil-for-Food Programme on 21 November 2003, the United Nations Office of the Iraq Programme was closed on 31 May 2004. The Office of Programme Planning, Budget and Accounts assumed the responsibility of completing the winding-up process, including the liquidation of advances by or reimbursement of expenditures to the implementing partners. As at 31 December 2004, full reimbursements were made to the specialized agencies and except for the Food and Agriculture Organization of the United Nations (FAO), all cash advances had been liquidated. As at 31 December 2004, the outstanding advances to FAO amounted to $9.38 million ($4.5 million as at 31 December 2005). Liquidation of the $4.5 million, however, would be dependent upon the resolution of claims filed by a third party against FAO. The Board noted that escrow financial statements for the financial period ended 31 December 2004 disclosed in note 9 of the notes to financial statements an estimated contingent liability between $6 million and $7 million to cover all claims and disputes involving the United Nations or its agencies with third parties.

3. United Nations system accounting standards

25. The Board assessed the extent to which the financial statements of the United Nations Escrow (Iraq) Account for the financial period ended 31 December 2004 conformed to the United Nations system accounting standards. The review indicated

that the presentation of the financial statements was generally consistent with the standards.

4. Accounts and financial reporting

Cancellation of expired letters of credit

26. The liability under a letter of credit automatically ceases to exist upon its expiration. In the case of the Oil-For-Food Programme, the United Nations Treasury has an existing arrangement with BNP Paribas to disable the automatic cancellation of the liability pending verification by the United Nations Treasury to ensure that there are no amendments of letters of credit in process with BNP Paribas, no outstanding deliveries are pending as confirmed by the Central Bank of Iraq, and that no authentication documents are in transit emanating from the United Nations Independent Inspection Agents.

27. The United Nations Treasury requires BNP Paribas to submit on a monthly basis an ageing report of letters of credit that have expired after a grace period of 90 days to avoid the unnecessary commitment of cash collateral. The list of expired letters of credit triggers the cancellation of the corresponding obligation. Should the buyer and seller agree to honour the contract, an amendment to extend the validity of the letter of credit is issued by BNP Paribas to the buyer for the reinstatement of the cash collateral.

28. Based on the BNP Paribas liability report as at 31 December 2004, the outstanding liability of the programme covering 923 letters of credit, inclusive of 294 to expire in 2005-2006, amounted to $2.85 billion, as follows:

Table 6
Outstanding liability

Date of expiration	*Number of letters of credit*	*Amount (in United States dollars)*
2002		
August	1	54 969.90
December	1	97 000.00
Subtotal	**2**	**151 969.90**
2003		
August	1	138.46
October	1	2 739 072.12
December	7	3 448 272.78
Subtotal	**9**	**6 187 483.36**
2004		
January	10	12 828 630.76
February	12	14 421 496.40
March	9	14 117 483.40
April	21	14 214 758.53

Date of expiration	*Number of letters of credit*	*Amount (in United States dollars)*
May	15	17 435 041.14
June	29	16 769 172.93
July	44	37 554 606.84
August	46	25 635 349.17
September	134	243 695 952.38
	320	**396 672 491.55**
	331	**403 011 944.81**
October	92	178 553 967.98
November	96	140 622 411.24
December	110	268 352 068.41
Subtotal	**618**	**984 200 939.19**
2005		
January	56	69 711 268.30
February	66	253 143 992.68
March	45	209 385 743.64
April	35	219 327 041.91
May	28	188 439 448.60
June	12	62 736 712.22
July	13	128 655 755.00
August	10	161 218 134.92
September	7	86 089 239.33
October	4	139 501 013.04
November	5	75 322 290.92
December	2	1 395 372.39
Subtotal	**283**	**1 594 926 012.95**
2006		
January	2	54 233 918.09
March	3	32 985 223.16
April	3	136 804 891.74
June	1	16 644 206.24
September	1	27 693 452.85
December	1	175 000.00
Subtotal	**11**	**268 536 692.09**
Grand total	**923**	**2 854 003 097.49**

29. As shown in table 6 above, a total of 331 letters of credit aggregating $403 million and with expiration dates from August 2002 to September 2004, remained outstanding per BNP liability report. Of these, the 129 that have expired after a grace period of 90 days were cancelled and the corresponding obligations were closed as at April 2005, while the remaining 202 letters of credit, aggregating $248.68 million, were still included in the liability report.

30. The non-cancellation of expired letters of credit unnecessarily tied up the equivalent cash collateral. Not immediately freeing unencumbered funds could also hamper the expeditious transfer of the remaining balances of the United Nations Escrow (Iraq) Account as envisioned in Security Council resolution 1483 (2003), while presenting a risk of being liquidated in error.

31. The Administration explained that certain expired letters of credit could not be cancelled owing either to the existence of valid claims or upon the request of the Iraqi authorities to keep the letters of credit active. It further explained that there were unusually long delays in the confirmation by the Central Bank of Iraq of the arrival of goods when the latter took full responsibility of authenticating deliveries. It has to consider these reasons before BNP is requested to cancel the relevant letters of credit.

32. The Administration informed the Board that the Office of Programme Planning, Budget and Accounts together with the Office of Legal Affairs is conducting an in-depth review of the whole question of extension of letters of credit, in the light of the complexities of the problem and taking into account the view of the Iraq Administration and other stakeholders.

33. **The Board recommends that the Administration continue to closely coordinate with BNP Paribas on the timely and practicable cancellation of letters of credit, which had expired, particularly in respect of those without valid claims.**

Unliquidated obligations

34. As at 31 December 2004, unliquidated obligations covering Funds ESB/ESC stood at $2,889 million, consisting of approximately $250 million for the current year and $ 2,639 million covering prior years. Comparatively, the BNP Paribas liability report as at that date reflected an outstanding liability of $2,854 million or a difference of about $35 million.

35. The Board reviewed 79 individual miscellaneous obligating documents and noted that 11 showed differences in balances when compared with the balances per BNP liability report, as presented in table 7 below.

Table 7
Comparison of balances of unliquidated obligations

Obligating document No.	*Fund ESB balance*	*Fund ESC balance*	*Total per books ESB and ESC*	*BNP balance (in United States dollars)*	*Difference over or (under)*
94547	73 198 668.85	0.00	73 198 668.85	73 585 928.86	(387 260.01)
96219	680 236.29	166 229.17	846 465.46	828 122.38	18 343.09
97628	246 416.51	0.00	246 416.51	243 897.56	2 518.95
85190	2 132 357.01	541 347.19	2 673 704.20	2 638 751.70	34 952.50
86262	7 509 946.58	0.00	7 509 946.58	7 496 110.19	13 836.39
86269	3 005 923.85	0.00	3 005 923.85	2 968 065.44	37 858.41
86591	5 060 950.49	506 462.73	5 567 413.22	6 171 890.83	(604 477.61)
86846	1 543 120.76	0.00	1 543 120.76	1 251 221.17	291 899.59
89919	60 604 129.64	0.00	60 604 129.64	60 250 897.44	353 232.20
77968	32 132 747.71	0.00	32 132 747.71	31 970 925.00	161 822.71
80250	16 728 441.96	0.00	16 728 441.96	16 632 752.05	95 689.91
Total net difference					**18 416.13**

36. In the case of obligating document No. 86591, the Board noted that the obligation as reflected in the BNP Paribas liability report was based on the original letter of credit, which amounted to €5.445 million instead of the amended contract price of €4.995 million. As a consequence, the overstatement of the unliquidated obligation also unduly committed cash collateral in the amount of €450,000. Accordingly, the Administration advised BNP to correct the overstatement.

37. Moreover, as shown in table 8 below, a total of 10 obligations outstanding as at 31 December 2004 and aggregating $5.7 million were not included in the BNP Paribas liability report.

Table 8
Outstanding obligations excluded from liability report

Obligating document No.	*Balance as at 31 December 2004 (in United States dollars)*	*Date closed in IMIS*
86499	274 935.08	04/04/05
97612	600 066.85	04/04/05
87384	621 859.76	04/04/05
88490	114 011.11	18/03/05
89669	185 430.69	18/03/05
91027	14 819.35	04/04/05
92700	1 238 445.54	04/04/05
80969	1 689 418.78	25/02/05
87132	320 675.89	18/03/05

Obligating document No.	*Balance as at 31 December 2004 (in United States dollars)*	*Date closed in IMIS*
85844	712 347.35	29/03/05
Total	**5 772 010.40**	

38. Certain reconciliations had been completed and the variances between IMIS and the BNP Paribas liability report had been identified. The Board noted, however, that the timing of those adjustments did not coincide with the appropriate financial period.

39. The Administration explained that reconciliations are carried out on a regular basis and would continue to be carried periodically. In the case of the differences covering the five above-mentioned obligating documents, it explained that they were due to foreign exchange differences. BNP Paribas records the payments using the bank exchange rates, whereas the United Nations records the same payments using the established United Nations operational exchange rate for a particular month. Owing to fluctuations in exchange rates, these differences are not reconciled until either final payment is made or the obligation is closed. Four obligating documents were closed in IMIS in 2005 as the 2004 financial period had already been closed. BNP Paribas was advised of the necessary correction.

40. **The Board recommends that the Administration continue to reconcile the balances of unliquidated obligations against the BNP Paribas liability report on a per-obligation basis and reflect the adjustment in the financial period to which it relates.**

41. The Administration requested the Board to reconsider the second part of the recommendation in view of the practical difficulties in recording all adjustments within the same financial period as the IMIS would be open for approximately six weeks within which known adjustments would be entered after 31 December but before issuance of the financial statements. In the opinion of the Board, however, the number of weeks IMIS would remain open for adjustments after 31 December does not matter. Of importance is the swift ability of the Administration to identify items requiring adjustments.

Accounting for cancelled letters of credit

42. Paragraph 11 of the United Nations system accounting standards provides, inter alia, that financial statements should have the qualitative characteristics required to make the information provided useful to the readers. One qualitative characteristic demands reliability of recorded information.

43. Rule 105.8 (b) of the Financial Regulations and Rules of the United Nations, in relation to paragraph 11 of the United Nations system accounting standards, states that when any obligation previously recorded in the accounts is, for any reason, reduced (other than by payment) or cancelled, the certifying officer shall accordingly ensure that appropriate adjustments are recorded in the accounts.

44. The Board's review of a sample of transactions covering the period from January to March 2005 and aggregating $96.8 million revealed that the amount of $31.1 million (table 9) represented letters of credit of prioritized and amended contracts which expired in 2004.

Table 9
Sample letters of credit which expired in 2004

Posted date	*Communication No.*	*Obligating document No.*	*Amount (in United States dollars)*
25/02/2005	1300208	92023	9 108 578.43
25/02/2005	1030043	95682	1 682 828.76
25/02/2005	801127	94663	2 828 193.30
25/02/2005	801254	95986	1 400 000.00
25/02/2005	1300153	91615	1 188 627.45
25/02/2005	1200123	89671	760 875.49
25/02/2005	900828	84707	1 389 945.10
25/02/2005	801252	74243	885 000.00
25/02/2005	601440	96684	2 873 984.08
25/02/2005	801253	76366	1 060 000.00
25/02/2005	801109	95982	700 000.00
25/02/2005	801110	95983	1 200 000.00
07/03/2005	601404	73368	6 043 165.09
Total			**31 121 197.70**

45. Following the 90-day grace period, BNP Paribas cancelled these letters of credit between the periods from 11 January to 16 February 2005. Cancellation memorandums were issued by the United Nations Treasury between 22 February and 5 March 2005 which took effect on those dates instead of the actual letters of credit expiry dates in 2004. Accordingly, since the closure of the obligations arising from the cancelled letters of credit was recorded only in 2005, the balance of unliquidated obligations as at 31 December 2004 was overstated by $31.12 million.

46. The Administration stated that owing to the delay in receiving authentication documents from the Central Bank of Iraq, the cancellation process took place in stages as the United Nations Treasury was still reviewing all expired letters of credit to ensure that there was no pending documentation before the list of cancellations was sent to BNP Paribas. Likewise, BNP Paribas reviewed its records to ensure that no documentation of performance regarding such letters of credit existed at their end before cancellations are effected.

47. **The Board recommends that the Administration ensure that transactions pertaining to a particular period are accurately recorded during the same period.**

Obligations raised/closed in 2005

48. Paragraph 30 of the United Nations system accounting standards provides, inter alia, that monetary items shall be reported using the United Nations operational rate of exchange in effect at the reporting date.

49. The Board examined the reserve for obligations covering transactions subsequent to the financial period ended 31 December 2004 and noted 28

obligations raised and 259 obligations closed, amounting to $37.05 million and $311.69 million, respectively, that were correctly posted in the 2004 accounting period.

50. The Board also noted that the currency amounts of 19 obligations, consisting of 5 obligations raised and 14 obligations closed were translated using exchange rates other than the exchange rate as at 31 December 2004, thus, understating the obligations by $314,016 and $355,740, respectively.

51. The Administration explained that they were aware of the technical issue within the batch programme which caused the slight discrepancies and that they would continue to review the issue with the IMIS team with several options having been considered.

52. **The Board recommends that the Administration coordinate with the IMIS Team regarding the currency exchange rates that would be used in the translation of balances of obligations raised or closed as at financial statement date.**

Adjustments on amended contracts

53. Table 10 presents price adjustments of 5 of the 68 amended contracts that were not correctly reflected in IMIS resulting in the understatement of the obligations by about $0.29 million as at 31 December 2004.

Table 10
Price adjustments of the amended contracts

Commission No.	*Obligating document No.*	*Currency*	*Exchange rate*	*Per contract (curr)*	*Per IMIS (curr)*	*Difference (translated amount)*
801547	77968	USD	1.00	110 327 309.00	110 340 996.04	(13 687.04)
900778	86262	EUR	0.737	23 732 235.00	23 742 432.42	(13 836.39)
731024	89042	EUR	0.737	3 376 576.00	3 405 792.94	(39 643.07)
1130047	87675	EUR	0.737	1 865 575.93	2 018 696.15	(207 761.49)
						(274 927.99)

54. The Administration stated that the variance pertaining to obligating document Nos. 77968 and 89042 was the result of applying different foreign exchange rates. Obligating document No. 86262 has two letters of credit that would necessitate the amendment of the contract amount. Obligating document No. 87675 has been under scrutiny on account of unresolved amendment issues.

55. The Administration further explained that obligations based on the status of letters of credit are reviewed by certifying officers in coordination with the United Nations Treasury although it conceded that obtaining an assurance that cancellation of obligations are proper is a tedious process.

56. **The Board recommends that the Administration continue to review the obligations related to amended contracts and effect the adjustments in IMIS in a timely manner.**

Long-outstanding liability

57. As at 31 December 2004, other accounts payable account of $728,281 under Fund ESE included an amount of $579,268 representing a deferred payable to the Government of Germany for the helicopter flights provided to UNSCOM (now UNMOVIC) in the early 1990s.

58. The Board noted that the non-settlement was due to conflicting opinions/interpretation that such reimbursement is in line with paragraph 8 (e) of Security Council resolution 986 (1995).

59. Considering that the account had remained outstanding since 1992, the Board is concerned as to the validity of the payable account.

60. **The Board recommends that the Administration in conjunction with UNMOVIC, resolve whether the payable to the Government of Germany represents a valid claim against the funds of the programme in order to clear the balance.**

5. Liabilities for end-of-service benefits

61. The estimated liabilities for end-for-service benefits are indicated in note 7 to the financial statements and amounted to $1.4 million for unpaid accrued vacation compensation and $1.3 million for unpaid repatriation grants and related expenditures of relocation entitlement, that is, a total of $2.7 million as at 31 December 2004.

6. Write-off of losses of receivables

62. Receivables amounting to $3,647.96 were written off against the funds covered in the United Nations Escrow (Iraq) Account established under the provisions of Security Council resolutions relating to Iraq. The amount consisted of receivables for the loss of unsold UNPA stamps held by the United Nations Office of the Humanitarian Coordinator in Iraq amounting to $3,539.96 and the cost of shipment of excess personal effects of $108.

7. Ex gratia payments

63. In accordance with financial rule 105.12, the Administration informed the Board that ex gratia payments totaling $156,712 were made during the financial period ended 31 December 2004 representing payments for medical expenses of $151,712 to a visiting relative of a United Nations Office of the Humanitarian Coordinator in Iraq staff member and compensation for the death of a contractor in the amount of $5,000.

8. Investigation of programme administration and management

64. An independent, high-level inquiry committee was tasked by the Secretary-General in April 2004 to investigate the administration and management of the programme, from its inception to its transfer to the Coalition Provisional Authority in Iraq. The terms of reference agreed between the Chairman of the Independent Inquiry Committee and the Secretary-General provided that the independent inquiry would collect and examine information relating to the administration and management of the programme, including allegations of fraud and corruption on the

part of United Nations officials, personnel and agents, as well as contractors, including entities that have entered into contracts with the United Nations or with Iraq under the programme.

65. The significant findings[1] published by the Independent Inquiry Committee in its series of reports were as follows:

Report	*Significant findings*
Interim report of 3 February 2005	(a) The selection process for each of the three United Nations contractors selected in 1996 did not conform to established financial and competitive bidding rules. The decision-making process in 1996 for the United Nations contractors did not meet reasonable standards of fairness and transparency. The consistent violation of prescribed procurement procedures, engaging in unfair practices, and failing to appropriately document decision-making processes, reflect adversely on one area of the United Nations administration; (b) The Office of the Iraq Programme Executive Director solicited and received on behalf of an oil buyer several barrels of allocation of oil from 1998 to 2001. His action and continuing conflict of interest were ethically improper, and seriously undermined the integrity of the United Nations. He denied having approached Iraqi officials and requesting oil allocation on behalf of an oil buyer. He failed to disclose the full nature of his contacts and relationship with a close friend as well as the full nature and extent of his communications with two individuals (one his close friend), regarding allocations under the programme. Further, his statements regarding the source of additional cash income, which he disclosed on his United Nations financial disclosure forms for the years 1999 to 2003 were not adequately supported by information; (c) Given the size and complexity of the programme, the resources committed to the internal audit of the programme were inadequate in comparison to the level of internal auditing staff for peacekeeping missions. Several important aspects of the programme were not reviewed by the Internal Audit Division. The Office of Internal Oversight Services reporting to the General Assembly on programme-related matters was unsatisfactory. The United Nations did not possess adequate means to resolve disputes regarding the activities of the Office of Internal Oversight Services, including disagreements relating to the scope of audits. Several deviations from best practices were evident. They included (i) inability to report directly to an audit committee or other independent board, (ii) failure to complete enterprise-wide risk assessment, and (iii) lack of budgetary independence; (d) The ESD account was not treated by the United Nations as a commission, either by design or practice, but rather as a necessary pool of funds dedicated to cover significant administrative expenses associated with the programme. Funds designated to be deposited in the account, pursuant to appropriate resolutions, were in fact deposited. Internal Audit Division conducted only one internal audit relating to the account. The accounting and financial reporting processes and results of the account were audited by the Board of Auditors.

[1] Based on reports published by the Independent Inquiry Committee on its website www.iic-offp.org.

Report	*Significant findings*	
Second interim report of 29 March 2005	(a)	There is no evidence that the selection of a humanitarian goods imports inspector in 1998 was subject to any affirmative or improper influence of the Secretary-General in the bidding or selection process;
	(b)	While an open bidding process took place, United Nations procurement rules relating to the qualification of prospective contractors were not appropriately followed;
	(c)	Evidence is not reasonably sufficient to show that the Secretary-General knew that a humanitarian goods inspector had submitted a bid on the humanitarian inspection contract in 1998;
	(d)	In the light of the newspaper article and the complaint of a conflict of interest because of the Secretary-General's son's employment, as well as the published information concerning the alleged illicit payments to a certain family, the inquiry initiated by the Secretary-General was inadequate, and the Secretary-General should have referred the matter to an appropriate United Nations department (Office of Internal Oversight Services and/or Office of Legal Affairs) for a thorough and independent investigation;
	(e)	The Secretary-General's son actively participated in efforts by a goods inspector to conceal the true nature of its continuing relationship with him and deceived the Secretary-General about this continuing financial relationship;
	(f)	The humanitarian goods inspector made false statements to the public, the United Nations, and the Independent Inquiry Committee;
	(g)	The former Under-Secretary-General for Management failed to take any action beyond the one-day inquiry that was conducted concerning the truth of the allegations and their ongoing impact on the fitness of the goods inspector to remain as a United Nations contractor.
Third interim report of 8 August 2005	(a)	The Office of the Iraq Programme Executive Director corruptly benefited from his request and receipt of Iraqi oil allocations and two individuals (one his close friend) financially benefited from and assisted in the Office of the Iraq Programme Executive Director's corrupt activity;
	(b)	The United Nations procurement officer and his friend corruptly participated in a scheme to solicit a bribe from one of the companies that submitted a bid for the oil inspection contract, in connection with the programme's oil inspection contact. However, the Committee does not have evidence that the company paid a bribe.
The management of the United Nations Oil-for-Food Programme of 7 September 2005	(a)	The Security Council failed to define clearly the practical parameters, policies and administrative responsibilities of the programme. The lack of clarity was exacerbated by permitting the Iraqi regime to exercise too much initiative in the programme design and its subsequent implementation. Compounding that difficulty, the Security Council, in contrast to most past practice, retained through the Committee established under its resolution 661 (1990) substantial elements of administrative control. Neither the Security Council nor the Secretariat leadership was in overall control;

Report	*Significant findings*
	(b) The administrative structure and the personnel practices of the Organization — certainly within the Secretariat — were simply not fit to meet the truly extraordinary challenges presented by the programme, or even programmes of much lesser scope. The Committee reports reveal serious instances of illicit, unethical, and corrupt behaviour within the United Nations, but the pervasive administrative difficulties were not only, or even primarily, related to personal malfeasance. As will become evident in the Committee's final report, the wholesale corruption within the programme took place among private companies, manipulated by the Iraqi regime;
	(c) Most notable among the United Nations structural faults is a grievous absence of effective auditing and management controls;
	(d) There was an absence of a sufficiently strong organizational ethic — an ethic that should permeate its leadership and staff if the United Nations is to command the respect upon which its work depends. The isolated instances of corruption extend to the top of the programme administration — one important reflection of the managerial weaknesses;
	(e) The particular nature of the programme placed in stark relief the difficulties of effective cooperation among United Nations agencies. There was and is no simple way accurately to track programme expenditures across agency lines.
Manipulation of the Oil-for-Food Programme by the Iraqi regime of 27 October 2005	(a) Iraq dispensed oil allocations to and on behalf of a wide array of individuals and groups whom it considered influential in their respective countries and who espoused pro-Iraq views or organized anti-sanctions activities. The Iraqi regime ultimately derived $228.8 million of illicit income from the payment of surcharges ("commissions" or "loading fees") in connection with oil contracts from 139 companies under the Oil-for-Food Programme;
	(b) Iraq derived more than $1.5 billion in income from "kickbacks" paid by 2,253 companies it selected to receive contracts for humanitarian goods under the programme. The payments made by those companies to the Iraqi regime were disguised by various subterfuges ("after-sales service fees" and "inland transportation fees") and were not reported to the United Nations by Iraq or the participating contractors;
	(c) The banking services agreement required the escrow bank to confirm all letters of credit issued by other banks under the programme and also allowed the escrow bank, including its branch, subsidiary and affiliate banks, principally in Geneva to issue letters of credit on behalf of private party oil purchasers. The escrow bank's loyalties were divided between serving the interests of the United Nations to promote transparency of transactions conducted under the programme and serving the interests of private clients to maintain the confidentiality of their business and financing arrangements, once the escrow bank chose to issue letters of credit for oil transactions;
	(d) The available evidence does not establish that the oil inspector systematically failed to perform in accord with its contractual obligations. Likewise, the review has not disclosed systematic non-performance of humanitarian goods inspectors of their contractual obligations. However, two investigative matters remain open with

Report	Significant findings
	respect to one of the two goods inspectors, which will be referred to the Office of Internal Oversight Services, Investigations Division, for further review;
	(e) The Committee does not find that the interactions of two former Humanitarian Coordinators with programme contractors violated existing Staff Regulations and Rules. Their activities, however, illustrate two distinct ethical dilemmas confronted by United Nations staff members — one involving post-employment activities and another involving responses to requests for official assistance from persons of their home countries;
	(f) There was no evidence that the former Secretary-General took part in or was aware of any corrupt activity.

9. Action taken by the Administration on the findings of the Independent Inquiry Committee

66. The Secretary-General responded to the definitive report before the security Council on 7 September 2005.

C. Management issues

1. Programme management

67. Based on the records of the Treasury of the United Nations as at April 2005, multiple extensions of the validity of the letters of credit were granted on account of the non-delivery of ordered items on scheduled shipment dates, as shown in table 11 below.

Table 11
Letters of credit with multiple extensions

Commission No	*Letter of credit No*	*Obligating document No*	*Letter of credit amendment No*	*Date amended*	*Latest shipment date*	*Validity date*
1001466	T736516	86765	2	24 Oct 03	01 Feb 04	01 Mar 04
			3	02 Dec 03	24 Feb 04	01 Apr 04
			4	06 Apr 04	01 Apr 04	01 Jun 04
			5	08 Sept 04	30 Dec 04	30 Jan 05
1100099	V735649	85632	8	06 Oct 04	30 Jan 04	02 Apr 04
			9	16 Jun 04	30 Jul 04	31 Aug 04
			10	26 Oct 04	30 Nov 04	30 Dec 04
1030563	T735378	86402	1	30 Dec 03	26 Sept 04	26 Nov 04
			2	21 Sept 04	26 Dec 04	28 Feb 05
1100123	V734225	98655	6	01 Dec 03	27 Dec 03	22 Feb 04
			7	09 Mar 04	—	01 May 04
			8	11 Aug 04	31 Aug 04	30 Sept 04
			9	20 Jan 05	15 Mar 05	15 Apr 05

Commission No.	*Letter of credit No.*	*Obligating document No.*	*Letter of credit amendment No.*	*Date amended*	*Latest shipment date*	*Validity date*
1030296	T734029	84887	4	17 Dec 04	27 Oct 04	27 Dec 04
			6	28 Feb 05	27 Dec 04	28 Feb 05
930480	L731945	82245	4	09 Dec 03	10 Sept 04	10 Nov 04
			5	27 Dec 04	31 Dec 05	31 Jan 06
801967	M739195	98650	1	11 Dec 03	21 Aug 04	21 Oct 04
			2	23 Sept 04	21 Mar 04	21 Dec 04

68. The Board believes that indefinite extensions are not consistent with the spirit of Security Council resolution 1483 (2003) mandating the Administration to fulfil all remaining obligations and ultimately turn over to the Government of Iraq all unencumbered balances. That view is shared by the former Controller of the United Nations in his letter of 16 December 2004 to the Permanent Representative of Iraq to the United Nations stating that in order to wind up the role of the United Nations in processing letters of credit, expired letters of credit will no longer be reinstated, no amendments to shipping dates would be extended after 31 December 2004, and funds associated with the corresponding letters of credit would be transferred to the Development Fund for Iraq.

69. The Administration explained that extensions of the validity of the letters of credit were based upon the agreement between the supplier, the buyer, the Authority and the Central Bank of Iraq. It had informed the Board that Iraqi authorities and certain Member States had requested the United Nations to assist Iraq and continue the processing of payments of the letters of credit. The Administration is reviewing the process relating to extensions, taking into account the practical complexities.

Payments of letters of credit

70. Shipments of humanitarian supplies and oil spares are subject to strict requirements as conditions for payment. In addition to authentication sheets, the Treasury of the United Nations issues "Secretary General's designee's standardized confirmation of arrival of goods in Iraq" authorizing BNP Paribas to initiate the payment process. BNP Paribas in turn prepares a payment sheet and submits the same to the United Nations Treasury for further verification, and if found in order, returns the duly payment sheet to BNP Paribas to effect the payment to the intended beneficiary. Those measures were intended to ensure that payments would be effected only for authorized transactions and beneficiaries.

71. The Board also noted that based on the review of 60 sample payments, the processing time ranged from one to seven days or an average time of 2.51 days per payment. Further, the orderly maintenance of files by the United Nations Treasury, which consisted of thousands of contracts for humanitarian supplies and oil spares, provided the assurance of the availability of supporting documents and ease of retrieval.

72. The Board encourages the United Nations Treasury to continue ensuring that processing and verification of payments including the filing of supporting documents remain efficient and effective.

Mandates of the United Nations Monitoring, Verification and Inspection Commission

73. As a subsidiary body of the Security Council UNMOVIC submitted a report on its activities to the Council at least quarterly. Much of its activities were focused on future monitoring through advance training and maintenance of a roster of experts/inspectors as well as working on the draft of a compendium of Iraq's prohibited weapons programmes. Activities related to the mandate include examination of commercially available satellite imagery, continuous assessment of sites known to have contained dual-use equipment and materials which could no longer be accounted for, and others.

74. The Board noted that UNMOVIC had approximately $345 million in total reserves and fund balances as at 31 December 2004 and only $17 million expenditures were incurred during the financial period ended 31 December 2004. The Board is concerned as to the optimum use of the resources of UNMOVIC considering that some of its goals and objectives may have been overtaken by events without its mandates being revisited as required in resolutions 1483 (2003) and 1546 (2004).

75. UNMOVIC officials were optimistic that following the Iraq election in January 2005 the Security Council would be inclined to revisit the said mandates.

2. Cases of fraud and presumptive fraud

76. Notwithstanding the results of the investigation by the Independent Inquiry Committee of the Oil-for-Food Programme, the Administration informed the Board that there were no known cases of fraud and presumptive fraud in the remaining activities of the programme, or in the operations of UNMOVIC during the period under audit.

D. Acknowledgment

77. The Board wishes to express its appreciation for the cooperation and assistance extended to the auditors by the Secretary-General of the United Nations, the Under-Secretary-General for Management, the Acting Executive Chairman, United Nations Monitoring, Verification and Inspection Commission and their officers and staff.

(*Signed*) Guillermo N. **Carague**
Chairman, Commission on Audit, Republic of the Philippines
(Lead Auditor)

(*Signed*) Shauket A. **Fakie**
Auditor-General of the Republic of South Africa

(*Signed*) Philippe **Séguin**
First President of the Court of Accounts of France

28 July 2006

Annex

Summary of status of implementation of recommendations for the financial period ended 31 December 2003

Topic	*Implemented*	*Under implementation*	*Overtaken by events*	*Total*	*Reference: paragraphs in present report*
Financial issues					
1. Cancellation of letters of credit and closure of obligations		Para. 38, Board report 2003 Annex A, Board report 2002 Para. 24, Board report 2001			24-31
2. Currency exchange adjustments in the reserve for obligations account		Para. 42, Board report 2003			45-49
Total (number)		**2**		**2**	
Total (per cent)		**100**		**100**	

Chapter II
Audit opinion

We have audited the accompanying financial statements of the United Nations Escrow (Iraq) Account comprising statements I to III and the supporting notes to the financial statements for the financial period ended 31 December 2004. These financial statements are the responsibility of the Secretary-General of the United Nations. Our responsibility is to express an opinion on the financial statements based on our audit.

We conducted our audit in accordance with the common auditing standards of the Panel of External Auditors of the United Nations, the specialized agencies and the International Atomic Energy Agency and with the International Standards on Auditing. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the Secretary-General, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for the audit opinion.

In our opinion, the financial statements present fairly, in all material respects, the financial position of the United Nations Escrow (Iraq) Account at 31 December 2004 and the results of its operations and its cash flows for the period then ended, in accordance with the United Nations system accounting standards.

Furthermore, in our opinion, the transactions of the United Nations Escrow (Iraq) Account that have come to our notice, or which we have tested as part of our audit, have in all significant respects been in accordance with the Financial Regulations and legislative authority.

Without qualifying our audit opinions expressed above, we draw attention to note 11 to the financial statements, which describes the results of the investigation conducted by the Independent Inquiry Committee in its interim reports of 3 February 2005 and 29 March 2005. The Independent Inquiry Committee noted that there were shortcomings in the procurement, management and internal oversight areas, and that certain actions of the former Executive Director of the programme were ethically improper. As at 31 March 2005, the Secretariat of the United Nations was in the process of considering the findings and recommendations of the Independent Inquiry Committee.

(*Signed*) Guillermo N. **Carague**
Chairman, Commission on Audit, Republic of the Philippines
(Lead Auditor)

(*Signed*) Shauket A. **Fakie**
Auditor-General of the Republic of South Africa

(*Signed*) Philippe **Séguin**
First President of the Court of Accounts of France

28 July 2006

Certification of the financial statements

1. The financial statements pursuant to Security Council resolution 986 (1995), and pursuant to Security Council resolutions 687 (1991), 706 (1991), 778 (1992), 1284 (1999), 1483 (2003) and 1546 (2004), for the period 1 January to 31 December 2004 have been prepared in accordance with financial rule 106.10.

2. The summary of significant accounting policies applied in the preparation of these statements is included as notes to the financial statements. These notes provide additional information and clarifications for the financial activities related to Security Council resolutions 687 (1991), 706 (1991), 778 (1992), 986 (1995), 1284 (1999), 1483 (2003) and 1546 (2004) undertaken by the Organization during the period covered by these statements for which the Secretary-General has administrative responsibility.

3. I certify that the appended financial statements of the United Nations Escrow Account, number I to III, are correct.

(*Signed*) Warren **Sach**
Acting Controller

31 March 2005

06-42637

United Nations Escrow Account established under the provisions of Security Council resolutions relating to Iraq a/

Statement of income and expenditures and changes in reserve and fund balances
for the twelve month period of the biennium 2004-2005 ending 31 December 2004
(Thousands of United States dollars)

	Security Council resolutions 986 (1995) and 1483 (2003)		Security Council resolutions 687 (1991), 706 (1991), 1284 (1999) c/	Security Council resolutions 687 (1991), 706 (1991) d/		
	Humanitarian activities in Iraq b/	**Administrative and operational costs**	**Monitoring, verification and inspection**	**Other activities**	**Total 2004**	**Total 2002**
Income						
Sale of Iraqi oil	-	-	-	-	-	10 240 332
Allocation to United Nations Compensation Commission	-	-	-	-	-	(2 587 641)
Subtotal	-	-	-	-	-	**7 652 691**
Interest income	104 655	3 874	5 559	-	114 088	603 095
Miscellaneous income	2 160	6 688	192	-	9 040	5 984
Currency exchange adjustments e/	-	34	1	-	35	892 619
Total income	**106 815**	**10 596**	**5 752**	**-**	**123 163**	**9 154 389**
Expenditure						
Purchase of humanitarian supplies f/	218 823	-	-	-	218 823	8 149 088
Purchase of spare parts g/	83 400	-	-	-	83 400	1 089 275
Pipeline tariff charges	-	-	-	-	-	193 142
Operational expenses by inter-agencies	-	2 497	-	-	2 497	127 809
Administrative expenses	-	12 023	16 671	232	28 926	105 547
Independent Inquiry Committee expenses h/	-	11 951	-	-	11 951	-
Interest expense	-	-	-	-	-	12 226
Currency exchange adjustments e/	23 234	-	-	-	23 234	14 945
Total expenditure	**325 457**	**26 471**	**16 671**	**232**	**368 831**	**9 692 032**
Excess (shortfall) of income over expenditure	**(218 642)**	**(15 875)**	**(10 919)**	**(232)**	**(245 668)**	**-537 643**
Prior-period adjustments	-	(4)	-	(4)	(8)	-
Net excess (shortfall) of income over expenditure	**(218 642)**	**(15 879)**	**(10 919)**	**(236)**	**-245 676**	**-537 643**
Savings on/or cancellation of prior period obligations i/	1 236 832	31 450	3 694	252	1 272 228	835 557
Transfers (to) from other organisations j/	(3 428 000)	(200 000)	-	-	(3 628 000)	-
Reserves and fund balances, beginning of period	2 613 358	298 303	353 096	619	3 265 376	5 247 209
Reserves and fund balances, end of period	**203 548**	**113 874**	**345 871**	**635**	**663 928**	**5 545 123**

a/ There were no activities relating to pipelines tariff charges and assets transfers and contributions during this period. Also see notes 3 and 4.

b/ Based on Security Council resolution 1483 (2003) amounts previously shown separately in respect of the "15 Governorates of Central and Southern Iraq" and "3 Governorates of Northern Iraq" have been combined under "Humanitarian activities in Iraq".

c/ Refers to the United Nations Monitoring Verification and Inspection Commission, see note 4.

d/ Refers to activities undertaken further to Security Council resolutions 687 (1991) and 706 (1991), see note 4.

e/ Represents currency exchange fluctuations between the Euro and the United States dollar and other currencies.

f/ Expenditure incurred during the biennium 2004-2005 for humanitarian supplies relates to adjustments and reinstatements of contracts entered into in previous years. The figure includes unliquidated obligations of $196 078 077.

g/ Expenditure incurred during the biennium 2004-2005 for spare parts relates to adjustments and reinstatements of contracts entered into in previous years. The figure includes unliquidated obligations of $54 103 262.

h/ See note 5.

i/ Effective 1 January 2002 prior period savings are available for allotment on a six-monthly basis.

j/ Transfers to Development Fund for Iraq held by the Central Bank of Iraq pursuant to Security Council resolution 1483 (2003).

The accompanying notes are an integral part of the financial statements.

Statement II

United Nations Escrow Account established under the provisions of Security Council resolutions relating to Iraq a/

Statement of assets, liabilities and reserves and fund balances as at 31 December 2004

(Thousands of United States dollars)

	Security Council resolutions 986 (1995) and 1483 (2003)		Security Council resolutions 687 (1991), 706 (1991), 1284 (1991)	Security Council resolutions 687 (1991), 706 (1991)		
	Humanitarian activities in Iraq	**Administrative and operational costs**	**Monitoring, verification and inspection**	**Other activities**	**Total 2004**	**Total 2002**
Assets						
Cash and term deposits	3 039 248	711	49		3 040 008	9 712 330
Short term investments						2 425 000
Cash pool	38 990 b/	115 233 c/	344 694 d/		498 926	4 764 913
Accounts receivable						
Inter-fund balances receivable e/				654	654	522 677
Accounts receivable from sale of Iraqi oil						1 243 871
Accounts receivable from inter-agencies	9 465 f/	13 f/	1 989		11 467	95 556
Other accounts receivable	5 471	57	108	10	5 596	67 251
Inter-office transactions pending processing		179	5		184	7
Deferred charges		6	1 654		1 660	5 052
Total assets	3 093 133	116 199	348 499	664	3 558 495	18 836 657
Liabilities						
Unliquidated obligations – current year	250 176 g/	195	1 791	10	252 172	6 775 712
Unliquidated obligations – prior years	2 638 922				2 638 922	5 203 653
Unliquidated obligations – future years						1 488
Frozen assets transfers and contributions payable						261 868
Accounts payable						
Inter-fund balances payable e/	143	1 441	61		1 645	885 398
Accounts payable to inter-agencies	344 h/	38	38		420	8 017
Other accounts payable		445	728	19	1 192	3 462
Accrued interest payable						149 532
Inter-office transactions pending processing		6			6	4
Total liabilities	2 889 585	2 325	2 628	29	2 894 567	13 291 534
Reserves and fund balances						
Operating reserves i/		48 000			48 000	
Cumulative surplus	203 548	65 874	345 871	635	615 928	5 545 123
Total reserves and fund balances	203 548	113 874	345 871	635	663 928	5 545 123
Total liabilities and reserves and fund balances	3 093 133	116 199	348 499	664	3 558 495	18 836 657

a/ There were no activities relating to pipelines tariff charges and assets transfers and contributions during this period. Also see notes 3 and 4.

b/ Represents share of United Nations Headquarters cash pool for the "Humanitarian activities in Iraq" comprising cash and term deposits $16,957,829, short-term investments $3,702,365 (market value $3,702,365), long-term investments $18,192,708 (market value $17,867,309), accrued interest receivable $146,479.

c/ Represents share of the United Nations Headquarters cash pool for "Administrative and operational costs", cash and term deposits $50,106,102, short-term investments $10,939,552 (market value $10,939,552), long-term investments $53,754,848 (market value $52,793,388), accrued interest receivable $432,508.

d/ Represents share of the United Nations Headquarters cash pool for "Monitoring, verification and inspection" cash and term deposits $149,880,919, short-term investments $32,725,163 (market value $32,723,163) long-term investments $160,795,306 (market value $157,919,320) and accrued interest receivable $1,294,644.

e/ See note 2(k)(iii).

f/ Represent the funds advanced to the United Nations inter-agencies implementing the humanitarian activities in accordance with Security Council resolution 986 (1995).

g/ Unliquidated obligation incurred during the 2004-2005 biennium for humanitarian supplies and spare parts relates to adjustments and reinstatements of contracts entered into in previous years.

h/ Represents amounts payable to United Nations inter-agencies for expenditures in excess of amounts advanced.

i/ See note 10.

The accompanying notes are an integral part of the financial statements.

United Nations Escrow Account established under the provisions of Security Council resolutions relating to Iraq a/

Statement of cash flows

for the twelve month period of the biennium 2004-2005 ending 31 December 2004

(Thousands of United States dollars)

	Security Council resolutions 986 (1995) and 1483 (2003)		Security Council resolutions 687 (1991) 706 (1991), 1284 (1999)	Security Council resolutions 687 (1991) 706 (1991)		
	Humanitarian activities in Iraq	**Administrative and operational costs**	**Monitoring, verification and inspection**	**Other activities**	**Total 2004**	**Total 2002**
Cash flows from operating activities						
Net excess (shortfall) of income over expenditure (statement I)	(218 642)	(15 879)	(10 919)	(236)	(245 676)	(537 643)
(Increase) decrease in accounts receivable from sales of Iraqi oil	-	-	-	-	-	(558 792)
(Increase) decrease in accounts receivable from inter-agencies	57 354	2 345	(586)		59 113	(30 817)
(Increase) decrease in other accounts receivable	4 522	682	613		5 777	61 949
(Increase) decrease in other assets	-	6	(5)		1	20
(Increase) decrease in inter-fund balances receivable	1 810	-	-	213	2 023	(316 435)
(Increase) decrease in deferred charges	-	2 580	(991)		1 589	1 402
Increase (decrease) in unliquidated obligations	(4 824 431)	(52 707)	(3 396)	(243)	(4 880 777)	(1 280 457)
Increase (decrease) in frozen assets transfers and contributions payable	-	-	-	-	-	(46 536)
Increase (decrease) in accounts payable to inter-agencies	(36 925)	(15 296)	(236)		(52 457)	(9 337)
Increase (decrease) in other accounts payable	(2 796)	(587)	(31)	14	(3 400)	(3 977)
Increase (decrease) in accrued interest payable	-	-	-	-	-	12 226
Increase (decrease) in inter-fund accounts payable	143	(2 656)	(1 593)		(4 106)	466 539
Less: Interest income	(104 655)	(3 874)	(5 559)		(114 088)	(603 095)
Net cash from operating activities	(5 123 620)	(85 426)	(22 703)	(252)	(5 232 001)	(2 844 953)
Cash flows from investing activities						
(Increase) decrease in short-term investments	-	-	-	-	-	2 767 080
(Increase) decrease in cash pool	679 491	249 276	13 278		942 045	(264 167)
Plus: Interest income	104 655	3 874	5 559		114 088	603 095
Net cash from investing activities	784 146	253 150	18 837		1 056 133	3 105 728
Cash flows from financing activities						
Savings on, or cancellation of prior period obligations	1 236 832	31 450	3 694	252	1 272 228	835 557
Transfers (to) from other organisations	(3 428 000)	(200 000)			(3 628 000)	
Net cash from financing activities	(2 191 168)	(168 550)	3 694	252	(2 355 772)	835 557
Net increase (decrease) in cash and term deposits	(6 530 642)	(526)	(172)		(6 531 640)	1 096 332
Cash and term deposits, beginning of period	9 569 890	1 537	221		9 571 648	8 615 998
Cash and term deposits, end of period c/	3 039 248	711	49		3 040 008	9 712 330

a/ There were no activities relating to pipelines tariff charges and assets transfers and contributions during this period. Also see notes 3 and 4.

b/ Reclassified to conform to current presentation.

c/ Cash and term deposits does not include cash and term deposits in the cash pool. Refer footnotes b/, c/ and d/ in statement II.

The accompanying notes are an integral part of the financial statements.

Notes to the financial statements for the United Nations Escrow Account established under the provisions of Security Council resolutions relating to Iraq

Note 1
The United Nations and its activities

(a) The Charter of the United Nations was signed on 26 June 1945 and came into force on 24 October 1945. The Organization's primary objectives, to be implemented through its five major organs, are as follows:

(i) The maintenance of international peace and security;

(ii) The promotion of international economic, social progress and development programmes;

(iii) The universal observance of human rights;

(iv) The administration of international justice and law;

(v) The development of self-government for Trust Territories;

(b) The General Assembly focuses on a wide range of political, economic and social issues as well as the financial and administrative aspects of the Organization;

(c) Under the direction of the Security Council, the Organization has been involved in various aspects of peacekeeping and peacemaking, including efforts towards resolving conflicts, restoring democracy, promoting disarmament, providing electoral assistance, facilitating post-conflict peacebuilding, and engaging in humanitarian activities to ensure survival of groups deprived of basic needs and overseeing the prosecution of persons responsible for serious violations of international humanitarian law;

(d) The Economic and Social Council plays a particular role in economic and social development, including a major oversight role in other organizations of the United Nations system to address international economic, social and health problems;

(e) The International Court of Justice has jurisdiction over disputes between Member States brought before it for advisory opinions or binding resolutions;

(f) The Trusteeship Council completed its primary functions in 1994 with the termination of the Trusteeship Agreement for the last United Nations Trust Territory.

Note 2
Summary of significant accounting and financial reporting policies of the United Nations

(a) The accounts of the United Nations are maintained in accordance with the Financial Regulations of the United Nations as adopted by the General Assembly, the rules formulated by the Secretary-General as required under the regulations and administrative instructions issued by the Under-Secretary-General for Management, or the Controller. They also take fully into account the United Nations system accounting standards, as adopted by the Administrative Committee

on Coordination, which has since been replaced by the United Nations System Chief Executives Board for Coordination. The Organization follows international accounting standard 1, "presentation of financial statements", on the disclosure of accounting policies, as modified and adopted by the Chief Executives Board for Coordination as follows:

(i) Going concern, consistency, and accrual are fundamental accounting assumptions. Where fundamental accounting assumptions are followed in financial statements, disclosure of such assumptions is not required. If a fundamental accounting assumption is not followed, that fact should be disclosed together with the reasons;

(ii) Prudence, substance over form and materiality should govern the selection and application of accounting policies;

(iii) Financial statements should include clear and concise disclosure of all significant accounting policies that have been used;

(iv) The disclosure of the significant accounting policies used should be an integral part of the financial statements. These policies should normally be disclosed in one place;

(v) Financial statements should show comparative figures for the corresponding period of the preceding financial period;

(vi) A change in an accounting policy that has a material effect in the current period or may have a material effect in subsequent periods should be disclosed together with the reasons. The effect of the change should, if material, be disclosed and quantified.

(b) The Organization's accounts are maintained on a fund accounting basis. Separate funds for general or special purposes may be established by the General Assembly, the Security Council or the Secretary-General. Each fund is maintained as a distinct financial and accounting entity with a separate self-balancing double-entry group of accounts. Separate financial statements are prepared for each fund or for a group of funds of the same nature;

(c) The financial period of the Organization is a biennium and consists of two consecutive calendar years for all funds other than peacekeeping accounts, which are reported on a fiscal year basis covering the period 1 July to 30 June;

(d) Generally, income, expenditure, assets, and liabilities are recognized on the accrual basis of accounting;

(e) The accounts of the Organization are presented in United States dollars. Accounts maintained in other currencies are translated into United States dollars at the time of the transactions at rates of exchange established by the United Nations. In respect of such currencies, the financial statements shall reflect the cash, investments, unpaid pledges, and current accounts receivable and payable in currencies other than the United States dollars, translated at the applicable United Nations rates of exchange in effect as at the date of the statements. In the event that the application of actual exchange rates at the date of the statements would provide a valuation materially different from the application of the Organization's rates of exchange for the last month of the financial period, a footnote will be provided quantifying the difference;

(f) The Organization's financial statements are prepared on the historical cost basis of accounting and are not adjusted to reflect the effects of changing prices for goods and services;

(g) The cash flow summary statement is based on the indirect method of cash flows, as referred to in the United Nations system accounting standards;

(h) The Organization's financial statements are presented in accordance with the ongoing recommendations of the Task Force on Accounting Standards to the United Nations System Chief Executives Board for Coordination;

(i) Income:

(i) Voluntary contributions from Member States or other donors are recorded as income on the basis of a written commitment to pay monetary contributions at specified times within the current financial period. Voluntary contributions made in the form of services and supplies that are acceptable to the Secretary-General are credited to income or noted in the financial statements;

(ii) Income received under inter-organization arrangements represents allocations of funding from agencies to enable the Organization to administer projects or other programmes on their behalf;

(iii) Allocations from other funds represent monies appropriated or designated from one fund for transfer to and disbursement from another fund;

(iv) Income for services rendered includes amounts charged for salaries of staff members and other costs that are attributable to the provision of technical and administrative support to other organizations;

(v) Interest income includes all interest earned on deposits in various bank accounts, investment income earned on marketable securities and other negotiable instruments, and investment income earned on the cash pool. All realized losses and net unrealized losses on short-term investments are offset against investment income. Investment income and costs associated with operation of investments in the cash pool are allocated to participating funds. Interest income is available for allotment purposes on a six-monthly basis;

(vi) Net gains or losses on currency fluctuations other than for current year's obligations are accumulated on a six-monthly basis. Effective 1 January 2002, the net amount is recognized as income or expenditure every six months in the financial statements;

(vii) Miscellaneous income includes income from rental of premises, sale of used or surplus property, refunds of expenditures charged to prior periods, settlements of insurance claims, monies accepted for which no purpose was specified, and other sundry income;

(viii) Income relating to future financial periods is not recognized in the current financial period and is recorded as deferred income as referred to in paragraph (l) (iii) below;

(j) Expenditure:

(i) Expenditures are incurred against authorized appropriations or commitment authorities. Total expenditures reported include unliquidated obligations and disbursements;

(ii) Expenditures incurred for non-expendable property are charged to the budget of the period when the property is acquired and are not capitalized. Inventory of such non-expendable property is maintained at historical cost;

(iii) Expenditures for future financial periods are not charged to the current financial period and are recorded as deferred charges as referred to in paragraph (k) (vi) below;

(iv) Expenditures include currency exchange adjustments on current period obligations;

(k) Assets:

(i) Cash and term deposits represent funds in demand deposit accounts and interest-bearing bank deposits;

(ii) Investments include marketable securities and other negotiable instruments acquired by the Organization to produce income. Short-term investments are stated at lower of cost or market; long-term investments are stated at cost. Cost is defined as the nominal value plus or minus any unamortized premium or discount. The market value of investments is disclosed in the footnotes to the financial statements;

(iii) Cash pool comprises participating funds' share of the cash and term deposits, short-term and long-term investments and accrual of investment income, all of which are managed in the pool. The investments in the pool are similar in nature and are accounted for as stated in item k (ii) above. Share in cash pool is reported separately in each of the participating fund's statement, and its composition and the market value of its investments are disclosed in footnotes in the individual statements;

(iv) Inter-fund balances reflect transactions between funds, and are included in the amounts due to and from the United Nations General Fund. Inter-fund balances also reflect transactions directly with other escrow accounts and with the United Nations General Fund. Inter-fund balances are settled periodically, dependent upon availability of cash resources;

(v) Provision for delays in collection of receivable balances is not made;

(vi) Deferred charges normally comprise expenditure items that are not properly chargeable in the current financial period. They will be charged as expenditure in a subsequent period. These expenditure items include commitments approved by the Controller for future financial periods in accordance with financial rule 106.7. Such commitments are normally restricted to administrative requirements of a continuing nature and to contracts or legal obligations where long lead times are required for delivery;

(vii) For purposes of the balance sheet statements only, those portions of education grant advances that are assumed to pertain to the scholastic years completed as at the date of the financial statement are shown as deferred charges. The full amounts of the advances are maintained as accounts receivable from staff members until the required proofs of entitlement are produced, at which time the budgetary accounts are charged, and the advances settled;

(viii) Maintenance and repairs of capital assets are charged against the appropriate budgetary accounts. Furniture, equipment, other non-expendable property, and leasehold improvements are not included in the assets of the Organization. Such acquisitions are charged against budgetary accounts in the year of purchase. The value of non-expendable property is disclosed in notes to the financial statements;

(l) Liabilities and reserves and fund balances:

(i) Operating reserves are included in the totals for "reserves and fund balances" shown in the financial statements;

(ii) Unliquidated obligations for future years are reported both as deferred charges and as unliquidated obligations;

(iii) Deferred income includes income received but not yet earned;

(iv) Commitments of the Organization relating to prior, current and future financial periods are shown as unliquidated obligations. Effective 1 January 2000, unliquidated obligations for the escrow account for humanitarian activities in Iraq remain valid until completion of the project. All other obligations continue to remain valid for 12 months following the end of the biennium to which they relate;

(v) Contingent liabilities, if any, are disclosed in the notes to the financial statements;

(vi) The United Nations is a member organization participating in the United Nations Joint Staff Pension Fund, which was established by the General Assembly to provide retirement, death, disability and related benefits. The Pension Fund is a funded defined benefit plan. The financial obligation of the Organization to the Pension Fund consists of its mandated contribution at the rate established by the General Assembly together with its share of any actuarial deficiency payments under article 26 of the Regulations of the Pension Fund. Such deficiency payments are payable only if and when the United Nations General Assembly has invoked the provision of article 26, following determination that there is a requirement for deficiency payments based on an assessment of the actuarial sufficiency of the Pension Fund as at the valuation date. As at the date of the current financial statement, the General Assembly has not invoked this provision.

Note 3
United Nations escrow account established under the provisions of Security Council resolution 986 (1995) (statements I, II and III)

(a) An escrow account to be administered by the Secretary-General was established in 1996 in order to receive the proceeds from sale of Iraqi oil as approved by Security Council resolution 986 (1995). The Security Council, in paragraph 1 of resolution 986 (1995), authorized States to permit the import of petroleum and petroleum products originating in Iraq, including financial and other essential transactions directly relating thereto, sufficient to produce a sum not exceeding a total of $1 billion every 90 days. In paragraph 3 the Security Council stated that the resolution shall remain in force for 180 days;

(b) The authorization given by paragraph 2 of resolution 986 (1995) permitted Turkey to import petroleum and petroleum products originating in Iraq, sufficient to meet the pipeline tariff charges for the transport of these products through the Kirkuk-Yumurtalik pipeline in Turkey, after deduction of 30 per cent to the Compensation Fund. Resolution 1330 (2000) revised this deduction to 25 per cent. Due to the cessation of the "Oil-for-Food Programme" (the programme), pipeline tariff charges are no longer incurred;

(c) The provisions of resolution 986 (1995), which authorized sales of Iraqi oil not exceeding a total of $1 billion every 90 days, remained in force by resolution 1111 (1997), resolution 1129 (1997), resolution 1143 (1997) and resolution 1158 (1998) until 30 May 1998;

(d) The Security Council, in paragraphs 1 and 2 of resolution 1153 (1998), which took effect on 1 June 1998, decided that the authorization given to States by paragraph 1 of resolution 986 (1995) shall permit the import of petroleum and petroleum products originating in Iraq, including financial and other essential transactions directly relating thereto, sufficient to produce a sum not exceeding a total of $5.256 billion, in the 180-day mandate period referred to in paragraph 1 of resolution 1153 (1998). This provision of resolution 1153 (1998), remained in force by resolution 1210 (1998), resolution 1242 (1999), and resolution 1281 (1999);

(e) Resolution 1284 of 17 December 1999 lifted the dollar cap and authorized sales of Iraqi oil of any volume during the 180-day mandate period. This resolution remained in force by resolution 1302 (2000), resolution 1330 (2000), resolution 1352 (2001) which extended resolution 1330 (2000) for 30 days, resolution 1360 (2001), resolution 1382 (2001), resolution 1409 (2002), resolution 1443 (2002) which extended 1409 (2002) until 4 December 2002, and resolution 1447 (2002) which extended the mandate to 3 June 2003. The final sale of oil under the Programme was for shipment made on 20 March 2003;

(f) The Security Council, in paragraphs 1 and 3 of its resolution 1175 (1998), authorized States to permit the export to Iraq of the necessary parts and equipment ("spare parts") to enable Iraq to increase the export of petroleum and petroleum products, in quantities sufficient to produce the sum established in paragraph 2 of resolution 1153 (1998). The resolution stated that the funds in the escrow account pursuant to resolution 1153 (1998) up to $300 million may be used to meet any reasonable expenses, other than expenses payable in Iraq, which follow directly from contracts approved by the Committee established by resolution 661 (1990). Resolutions 1293 (2000) and 1302 (2000) established that up to $600 million may be authorized to permit States to export to Iraq the necessary parts and equipment to enable Iraq to increase the export of petroleum and petroleum products. Resolutions 1330 (2000), 1352 (2001), 1360 (2001), 1382 (2001), 1409 (2002) and 1447 (2002) retain the $600 million limit;

(g) Resolution 1330 (2000) allowed for funds up to €600 million from the escrow account to be used for the installation, maintenance, and training services of spare parts and equipment relating to the oil industry;

(h) The Security Council, in its resolution 1472 (2003), recognized that in view of the exceptional circumstances prevailing in Iraq, on an interim and exceptional basis, technical and temporary adjustments should be made to the

programme, and authorized the Secretary-General to make such changes for a period of 45 days;

(i) The Security Council, in its resolution 1476 (2003), decided that the provisions contained in paragraph 4 of resolution 1472 (2003) remain in force until 3 June 2003 and might be subject to further renewal by the Council;

(j) The Security Council, in its resolution 1483 (2003), requested the Secretary-General to terminate the programme within six months, and to transfer responsibility for the administration of any remaining activity to the Coalition Provisional Authority (the Authority). The Council also requested the consolidation of the accounts established pursuant to paragraphs 8 (a) "15 Governorates of Central and Southern Iraq", and 8 (b) "3 Governorates of Northern Iraq" of resolution 986 (1995);

(k) Sale of Iraqi oil is recognized as revenue in the fund for humanitarian activities in Iraq based on the bill of lading date and the total value of oil loaded as stipulated in the commercial invoice issued by the State Oil Marketing Organization. The proceeds from sale of Iraqi oil are allocated, upon receipt of deposits, to other accounts established pursuant to paragraph 8 of resolution 986 (1995). No oil sales were recorded after 20 March 2003;

(l) The funds from the sale of Iraqi oil pursuant to the authorization given by paragraph 1 of resolution 986 (1995) are to be used to meet the humanitarian needs of the Iraqi people and for the other purposes in paragraph 8 of resolution 986 (1995). In its resolution 1409 (2002), the Security Council permits the sale or supply of any commodities or products other than those referred to in paragraph 24 of resolution 687 (1991) as it relates to military commodities and products, or military-related commodities or products covered by the Goods Review List (S/2002/515) and its amendments in resolution 1454 (2002). The percentages used in allocating the oil sale proceeds were determined as follows:

(i) 53.034 per cent to finance the export to Iraq of medicine, health supplies, food, and materials and supplies for essential civilian needs. Pursuant to resolution 1302 (2000) this was increased to 54.034 per cent and by resolution 1330 (2000) further increased to 59.034 per cent, less the payment referred to in paragraph (vi) below;

(ii) 13.0 per cent to complement the distribution by the Government of Iraq of goods imported by providing funds to the United Nations inter-agency humanitarian programme operating in the three northern governorates of Iraq, Arbil, Dihouk and Sulaimaniyeh;

(iii) 2.215 per cent to meet the operational and administrative costs to the United Nations;

(iv) 30.0 per cent allocated to the Compensation Fund established by the Security Council in its resolution 705 (1991). Pursuant to resolution 1330 (2000) this was decreased to 25.0 per cent;

(v) 0.751 per cent allocated to the United Nations Monitoring, Verification and Inspection Commission (UNMOVIC) established by the Security Council in resolution 1284 (1999), which replaced the Special Commissions established by Security Council resolution 687 (1991) to meet operating costs;

(vi) A maximum of $10 million every 90-day period to be allocated to the escrow account established by the Security Council in its resolutions 706 (1991) and 712 (1991) for the payments envisaged under paragraph 6 of resolution 778 (1992). In resolution 1284 (1999), the Council suspended payments to this escrow account for an initial period of six months from 17 December 1999. In resolution 1302 (2000), the Council extended this suspension for a further 180-day period and transferred the allocation referred to (i) above. In resolution 1330 (2000), the Council reinstated the allocation of a maximum of $10 million every 90 days from 6 December 2000;

(m) Notwithstanding the periods for the sale of Iraqi oil as authorized by Security Council resolutions, the financial statements I, II and III (United Nations Escrow Account) are prepared every six months;

(n) Included in financial statements I, II and III (United Nations Escrow Account) are details relating to the humanitarian activities, related operational and administrative costs, and pipeline tariff charges, that are undertaken under the provisions of Security Council resolution 986 (1995). The financial statements of the Compensation Fund as referenced in paragraph (l) (iv) above are reported on in a separate volume of the United Nations financial statements;

(o) Expenditure incurred during the biennium 2004-2005 for humanitarian supplies and spare parts relate to adjustments and reinstatements of contract entered into in previous years.

Note 4
United Nations Escrow Account established under the provisions of Security Council resolutions 687 (1991), 706 (1991), 778 (1992) and 1284 (1999) (statements I, II and III)

(a) Included in financial statements I, II and III are the escrow accounts established by the Security Council in resolutions 706 (1991) and 712 (1991) for the payments envisaged under paragraph 6 of resolution 778 (1992), and the Special Account established by the Security Council in resolutions 687 (1991), 706 (1991) and 1284 (1999). These accounts were previously included in a separate volume. All comparative figures have been restated. The escrow account established under Security Council resolutions 706 (1991), 712 (1991) and 778 (1992) returned all funds in 2003. As a result, there are no further transactions to report relating to this escrow account;

(b) The escrow account administered by the Secretary-General under Security Council resolutions 706 (1991) and 712 (1991) provided for Iraqi funds from the sale of oil to be used for payment by the United Nations Compensation Commission, the full costs of carrying out the tasks authorized by section C of resolution 687 (1991), the full costs incurred by the United Nations in facilitating the return of all Kuwait property seized by Iraq, half the costs of the Boundary Commission, and the cost to the United Nations of implementing resolution 706 (1991), and of other necessary humanitarian activities in Iraq;

(i) With the refusal of Iraq to sell oil under the provisions of Security Council resolutions 706 (1991) and 712 (1991), the Security Council on 2 October 1992 adopted resolution 778 (1992) as an alternative means of providing funds for the purposes specified. Member States in which there were

petroleum products owned by Iraq or Member States with funds of the Government of Iraq representing the proceeds of petroleum sales, paid for by the purchaser after 6 August 1990, were required to transfer some or all of these funds to the escrow account. Additionally, in resolution 778 (1992) the Council urged Member States to contribute funds from other sources to the escrow account. All such funds transferred or contributed to the escrow account under the provisions of resolution 778 (1992) were to be transferred back to the accounts of States from which funds were provided, together with applicable interest, at such time when oil exports have taken place pursuant to the system provided in resolutions 706 (1991) and 712 (1991) and the escrow account has received funds from the proceeds of sale. Iraqi oil exports began in December 1996 and in January 1997 the escrow account started receiving funds from the proceeds of sale which were transferred back to the accounts of States that provided the original funds to the escrow account;

(ii) In December 1999, pursuant to Security Council resolution 1284 (1999), payment to the escrow account from the proceeds of sales was suspended. The suspension, which was extended an additional 180 days by the Security Council in resolution 1302 (2000), was lifted by the Security Council in resolution 1330 (2000) in December 2000;

(iii) In May 2003 the Security Council in resolution 1483 (2003) requested the Secretary-General to restore funds that were provided by Member States pursuant to resolution 778 (1992). All such funds were returned in June 2003;

(c) The Security Council in resolution 687 (1991) requested the Secretary-General to undertake certain tasks in connection with the situation between Iraq and Kuwait. The costs of those activities were to be considered as an advance pending the receipt of payments to the Organization by Iraq in respect of certain activities, and by Iraq and Kuwait jointly in respect of the costs of the Boundary Commission;

(i) With the adoption by the Security Council of resolution 778 (1992), the above-mentioned costs have been covered by transfers from the escrow account. Furthermore, the costs of the Special Commission are met by transfer from the escrow account pursuant to Security Council resolution 986 (1995);

(ii) The Security Council decided by resolution 1284 (1999) to establish the United Nations Monitoring, Verification and Inspection Commission (UNMOVIC). The responsibilities mandated to the Special Commission are undertaken by UNMOVIC;

(iii) The Security Council in resolutions 1483 (2003) and 1546 (2004) reaffirmed the Council's intention to revisit the mandate of UNMOVIC.

Note 5
Independent Inquiry Committee into the United Nations Oil-for-Food Programme expenditure

The Security Council in its resolution 1538 (2004) welcomed the Secretary-General's appointment of an independent high-level inquiry to investigate allegations concerning the United Nations Oil-for-Food Programme. Costs of the Committee are met from funds for administrative and operational costs of the programme. Expenditures during the twelve-month period of the biennium 2004-2005 ending 31 December 2004 were:

	(Thousands of United States dollars)
Salaries	4 139.8
Consulting fees	5 148.9
Travel	1 270.6
Communication	72.8
Premises	222.5
Equipment	1 023.8
Miscellaneous supplies and services	72.5
Total	**11 950.9**

Note 6
Non-expendable property

In accordance with United Nations accounting policies, non-expendable property is charged against the current allotment in the year of purchase. The non-expendable property valued at historical cost, according to the cumulative inventory records is:

	2004	*2002*
	(Thousands of United States dollars)	
UNOHCI		5 746.0
UNMOVIC	9 954.2	1 179.2
Agencies[a]	2 717.0	20 976.7
United Nations Office of the Humanitarian Coordination in Iraq		1
Independent Inquiry Committee	837.1	—

[a] Due to evacuation of United Nations personnel from Iraq, it was not possible to fully ascertain the value of non-expendable property in Iraq as at 31 December 2004.
[b] Previously included in financial statements of the United Nations General Fund and related funds, volume I.

Note 7
Liabilities for end-of-service benefits

(a) Staff members who separate from the Organization are entitled to be paid for any unused vacation days they may have accrued up to a maximum of 60 days. The Organization's total liability for such unpaid accrued vacation compensation for staff working in the various activities related to Security Council resolutions 687 (1991), 706 (1991), 778 (1992), 986 (1995), 1284 (1999) and 1483 (2003) as of 31 December 2004 is estimated at $1.4 million.

(b) Some staff members are entitled to repatriation grant and related expenditures of relocation upon their separation from the Organization based on the number of years of service. The Organization's total liability for such unpaid repatriation and relocation entitlement for staff working in the various activities

related to Security Council resolutions 687, 706, 778, 986, 1284 and 1483 as of 31 December 2004 is estimated at $1.3 million.

Note 8

Future modus operandi of United Nations Escrow Account established under Security Council resolution 986 (1995)

(a) The Security Council in resolution 1483 (2003), extended the Secretary-General's responsibilities under Council resolutions 1472 (2003) and 1476 (2003) for a period of six months. The Council requested the Secretary-General to terminate, in the most cost-effective manner, the ongoing operations of the programme at Headquarters and in the field by 21 November 2003, and to transfer responsibility for the administration of any remaining activity under the programme to the Authority;

(b) Accordingly, in the three Governorates of northern Iraq where the United Nations agencies were implementing the programme, contracts entered into by the agencies were transferred to the Authority. Similarly, in the 15 Governorates of central and southern Iraq, where, after the outbreak of hostilities agencies had been assigned responsibility for procurement activities previously undertaken by the Government of Iraq, uncompleted contracts were handed over to the Authority;

(c) The Security Council in resolution 1546 (2004) decided that in connection with the dissolution of the Authority, the Interim Government of Iraq and its successors shall assume the rights, responsibilities and obligations relating to the programme that were transferred to the Authority, including all operational responsibility for the programme and any obligations undertaken by the Authority in connection with such responsibility, and responsibility for ensuring independently authenticated confirmation that goods have been delivered, and further decided that following a 120-day transition period from the date of adoption of the resolution, the Interim Government of Iraq and its successors shall assume all responsibility for certifying delivery of goods under previously prioritized contracts, and that such certification shall be deemed to constitute the independent authentication required for the release of funds associated with such contracts, consulting as appropriate to ensure the smooth implementation of those arrangements;

(d) As of 31 December 2004, the liquidation of the programme continued. All obligations relating to contracts that had not been prioritized in accordance with Security Council resolution 1483 (2003) had been closed, except for those where letters of credit had not lapsed. Obligations relating to contracts that had been prioritized remain as liabilities of the programme, and the related letters of credit have not been closed. The expiry dates for the letters of credit extend until 2007. As at 31 December 2004, $9.228 billion was transferred to the Development Fund for Iraq, with $3.628 billion being transferred during 2004. The remaining surplus funds will be returned to the Development Fund for Iraq in accordance with the provisions of paragraph 17 of resolution 1483 (2003). In that respect, and with the cancellation of further contracts and their related obligations during the first quarter of 2005, an additional sum of $450 million has already been transferred to the Development Fund for Iraq.

Note 9
Contingent liabilities

In accordance with Security Council resolution 1483 (2003), as part of the liquidation process, all claims and disputes involving the United Nations or its agencies with third parties, in carrying out the activities of the programme are to be transferred to, and become the responsibility of, the Authority. There may be some circumstances where such a transfer is not possible and any liability and related fees will need to be met by the programme. The amount is estimated at between $6 million and $7 million.

Note 10
Operating reserves

An operating reserve of $48 million was established during the period ended 31 December 2004 under "Administrative and operational costs". The reserve is to meet compensation costs payable in respect of those Oil-for-Food Programme staff members who were injured or killed as a result of the bombing of the United Nations Headquarters building in Baghdad on 19 August 2003, as well as to set aside funds to meet the expected costs of the Independent Inquiry Committee into the Oil-for-Food Programme and the administrative costs of the escrow accounts until all aspects of the programme have been completed.

Note 11
Investigation by the Independent Inquiry Committee

In April 2004, the Secretary-General appointed a high-level Independent Inquiry Committee to investigate the administration and management of the Oil-for-Food Programme from its inception to its transfer to the Coalition Provincial Authority, including allegations of fraud and corruption on the part of United Nations officials, personnel and agents as well as contractors, including entities that have entered into contracts with the United Nations or with Iraq under the programme. Following this, the Security Council adopted resolution 1538 (2004), in which it welcomed the inquiry.

The Committee recognized that the programme was unique to the United Nations in many aspects, namely, its sheer size, scope and political and geographic complexities. As of 31 March 2005, two interim reports dated 3 February 2005 and 29 March 2005 had been issued, and the Committee's inquiry was ongoing. The Committee's interim findings were that, inter alia, there were shortcomings in the procurement, management and internal oversight areas and that certain actions of the former Executive Director of the Programme "were ethically improper". The Committee also made interim recommendations related to the programme.

As at 31 March 2005, the Secretariat was in the process of considering the findings and recommendations in the Committee's interim reports.

United Nations S/2006/673

Security Council

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Note by the Secretary-General

The Secretary-General has the honour to transmit herewith to the Security Council the report of the Board of Auditors on the financial statements of the United Nations Escrow (Iraq) Account for the biennium ended 31 December 2005.

06-42731 (E) 220906

Report of the Board of Auditors on the audit of the accounts of the United Nations Escrow (Iraq) Account established under the provisions of Security Council resolutions 986 (1995), 706 (1991), 778 (1992), 687 (1991), 1284 (1999) and 1483 (2003) for the biennium ended 31 December 2005

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31 March 2006

Dear Mr. Chairman,

In accordance with financial regulation 6.5, I have the honour to submit the accounts of the United Nations Escrow Account established pursuant to Security Council resolution 986 (1995), and pursuant to Security Council resolutions 687 (1991), 706 (1991), 778 (1992), 1284 (1999), 1483 (2003) and 1546 (2004), for the biennium 2004-2005 ending 31 December 2005, which I hereby approve. The financial statements have been completed and certified as correct by the Controller.

(*Signed*) Kofi A. **Annan**

Mr. Guillermo N. Carague
Chairman
United Nations Board of Auditors
New York

I. Report of the Board of Auditors

Executive summary

The Board of Auditors has audited the operations of the United Nations Escrow Account established under the provisions of Security Council resolutions relating to Iraq for the biennium 2004-2005 ended 31 December 2005. The Board has also audited the financial statements of the United Nations Escrow Account (statements I, II and III) for the biennium ended 31 December 2005, taking into account the audit assurance obtained when the Board expressed an opinion on the 2004 financial statements of the escrow (Iraq) account.

The Board issued an unqualified opinion on the financial statements for the United Nations Escrow (Iraq) Account for the biennium ended 31 December 2005, as reflected in chapter II.

Implementation of previous recommendations

The Board has indicated in the annex to the present chapter, the summary status of implementation of recommendations for the period 1 January to 31 December 2003. The two recommendations previously reported were still under implementation by the Administration.

Financial overview for the biennium ended 31 December 2005

As at 31 December 2005, cash and term deposits and cash pool amounted to $1.56 billion. They adequately covered the $1.28 billion unliquidated obligations arising from approved contracts for current and prior periods. The total reserves and fund balances decreased considerably by $2.99 billion from $3.27 billion in 2003 to $28 million in 2005. The decrease was attributed to the transfer of funds to the Development Fund for Iraq. Shortfall of income over expenditure for the biennium was registered at $165.73 million, compared to the surplus of $286 million for the biennium 2002-2003.

Total income significantly decreased by 98 per cent from 2003 to 2005. The bulk of income in 2003 came from sale of Iraqi oil. That proportion was reduced owing primarily to the stoppage of oil sales on 20 March 2003. The closure of the programme in November 2003 and the transfer of funds to the Development Fund for Iraq during the biennium 2004-2005 had drastically reduced the funds of the programme. Cash pool, which is the major source of interest income for Iraq accounts, has dropped by $1.27 billion, or 88 per cent, from its balance of $1.44 billion in the biennium ending 2003 to $0.17 billion in the biennium ending 2005. Correspondingly, there was a decrease of 83 per cent in interest income from $999 million during the biennium 2002-2003 to $166 million during the biennium 2004-2005.

Programme implementation

The non-cancellation of the expired letters of credit hampered the complete liquidation of the programme and held up cash collaterals associated with each expired letter of credit.

Revisit of mandate of the United Nations Monitoring, Verification and Inspection Commission

As at 31 December 2005, a reserve of $114 million remained in the escrow account for the activities of the United Nations Monitoring, Verification and Inspection Commission (UNMOVIC). During the biennium ended 31 December 2005, administrative expenditure amounted to $32 million. That may not be in keeping with the proper management of UNMOVIC resources considering that most of its goals and objectives have already been overtaken by events without its mandate being revisited pursuant to Security Council resolution 1546 (2004).

Non-expendable property

There were no accurate values of the non-expendable property of UNMOVIC reported as lost and missing during the Baghdad bombings and lootings.

Recommendations

The Board has made the following recommendations for the Administration to:

(a) Make representation to the Security Council and the Government of Iraq to finally resolve the issue on contracts with expired letters of credit;

(b) Continue to coordinate closely with the designated bank for the release of the cash collateral associated with each expired letter of credit in order to adjust the unliquidated obligations at the time the cash collateral is released by the bank;

(c) Initiate evaluation of the UNMOVIC mandate in the light of current events and again invite the Security Council to decide the final course of action to take; and

(d) Facilitate completion of the final inventory necessary to update the UNMOVIC records of non-expendable property lost or stolen.

A. Introduction

1. The Board of Auditors has audited the financial statements of the United Nations Escrow (Iraq) Account established under the provisions of Security Council resolutions relating to Iraq, in accordance with Security Council resolutions 986 (1995), 1483 (2003), and 1546 (2004), and pursuant to Council resolutions 687 (1991), 706 (1991), 778 (1992), and 1284 (1999). Security Council resolution 1483 (2003) calls for the termination of the Oil-for-Food Programme.

2. The audit was conducted in conformity with article VII of the United Nations Financial Regulations and Rules and the annex thereto, and the common auditing standards of the Panel of External Auditors of the United Nations, the specialized agencies and the International Atomic Energy Agency and the International Standards on Auditing. Those standards require that the Board plan and perform the audit to obtain reasonable assurance that the financial statements are free of material misstatements. The present report is addressed to the Secretary-General who is invited to forward it to the President of the Security Council.

3. The audit was conducted primarily to enable the Board to form an opinion as to whether the unliquidated obligations recorded in the financial statements for the period from 1 January to 31 December 2005 had been incurred in pursuance of the provisions of resolution 1483 (2003), whether income and expenditures and other accounts were properly classified and recorded in accordance with the Financial Regulations and Rules, and whether the financial statements of the United Nations Escrow (Iraq) Account presented fairly the financial position as at 31 December 2005. The audit included a general review of the financial systems and tests of the adequacy of the existing controls, and a test examination of accounting records and other supporting evidence, to the extent the Board considered necessary to form an opinion on the financial statements.

4. The Board continued to report the results of the audit to the Administration in management letters containing detailed observations and recommendations. That practice allowed for ongoing dialogue with the Administration.

5. The present report covers matters that, in the opinion of the Board, should be brought to the attention of the General Assembly. The Board's observations and recommendations were discussed with the Administration, whose views have been appropriately addressed in the present report.

1. Previous recommendations not fully implemented

Period ended 31 December 2003

6. The Board reviewed the measures taken by the Administration to implement the recommendations made in its report for the period ended 31 December 2003. The two recommendations contained in the report were under implementation. Details of the action taken and the comments of the Board are included in the relevant discussion within the present report.

2. Recommendations

7. **The Board's recommendations are that the Administration:**

(a) **Strongly urge the Security Council and the Government of Iraq to finally resolve the issue of contracts with expired letters of credit (para. 31 (a));**

(b) **Continue to coordinate closely with the designated bank for the release of the cash collateral associated with each expired letter of credit in order to adjust the unliquidated obligations at the time the cash collateral is released by the bank (para. 31 (b));**

(c) **Initiate the evaluation of the UNMOVIC mandate in the light of current events and again invite the Security Council to steer the final course of action to take (para. 46);**

(d) **Facilitate completion of the final inventory necessary to update UNMOVIC records of non-expendable property lost or stolen (para. 51).**

3. Background

8. In view of the termination of the Oil-for-Food Programme effective 21 November 2003, the United Nations Office of the Iraq Programme authorized the transfer of responsibility for the administration of its remaining activities to the Coalition Provisional Authority in Iraq pursuant to Security Council resolution 1483 (2003). The Coalition Provisional Authority ceased to exist when the occupation ended on 30 June 2004 and the interim Government of Iraq assumed full responsibility and authority.

9. The remaining obligations related to approved and funded contracts earlier concluded by the previous Government of Iraq and were covered by letters of credit. The letters of credit issued by the designated bank for the purpose of humanitarian supplies were irrevocable and non-transferable and were continuously administered by the United Nations beyond 21 November 2003. The United Nations, aside from keeping the collateral for the full value of the letters of credit, also retained responsibility for their administration until they were executed or expired.

Humanitarian supplies

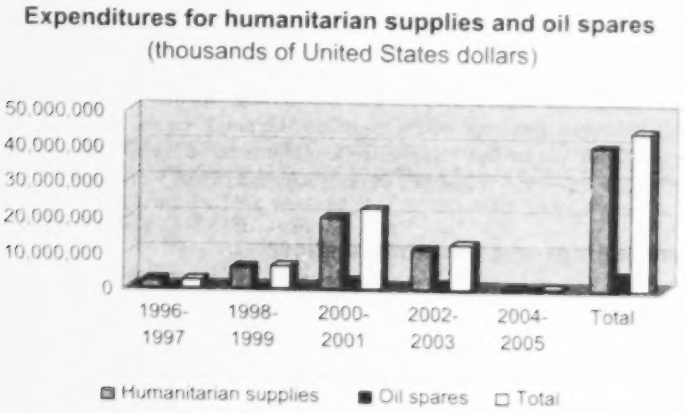
10. On 22 May 2003, by resolution 1483 (2003), the Security Council lifted the civilian sanctions against Iraq. In accordance with paragraph 16 of the resolution, the United Nations, in coordination with the Coalition Provisional Authority and the relevant Iraqi authorities, reviewed the relative utility of each contract still in the pipeline and in exceptional cases also included those unfunded contracts.

11. The Security Council in its resolution 1546 (2004) decided that in connection with the dissolution of the Coalition Provisional Authority, the Interim Government of Iraq and its successors shall assume the rights, responsibilities and obligations relating to the programme that were transferred to the Coalition Provisional Authority, including all operational responsibility for the programme and any obligations undertaken by the Coalition Provisional Authority in connection with such responsibility, and the responsibility for ensuring independently the authenticated confirmation that goods have been delivered.

12. As at 31 December 2005, the liquidation of the programme continued. All obligations relating to contracts that had not been prioritized in accordance with Security Council resolution 1483 (2003) had been closed, except for those where letters of credit had not lapsed. Obligations relating to contracts that had been prioritized remained as liabilities of the programme. The expiry dates of the letters of credit were extended until 2007. In his letters dated 8 August 2005, 17 October 2005 and 19 December 2005, the Secretary-General kept the Security Council informed of the arrangements for the liquidation of the outstanding letters of credit, and indicated that progress had been made on the amendments of the letters of credit by the relevant authorities of the Government of Iraq while little progress had been made in regard to the processing of authentication documents. The Security Council has taken note of the matter.

13. As at 9 October 2004, the Interim Government of Iraq has designated the Central Bank of Iraq as the institution responsible for the certification of the delivery of goods in Iraq. The Central Bank of Iraq worked with the buyers in Iraq who received the goods in order to prepare and forward such certification directly to the United Nations. The United Nations Treasury in turn reviewed the authentication documents before forwarding them to the designated bank for final payment. The Board reviewed on a sampling basis the completeness and validity of the authentication documents submitted to the United Nations Treasury by the Central Bank of Iraq for 2005 expenditures amounting to $280 million. During the biennium 2004-2005, the Oil-for-Food Programme spent $582 million on humanitarian supplies and oil spares. As at 31 December 2005, total expenditures reached $44 billion as shown in figure I below:

Figure I

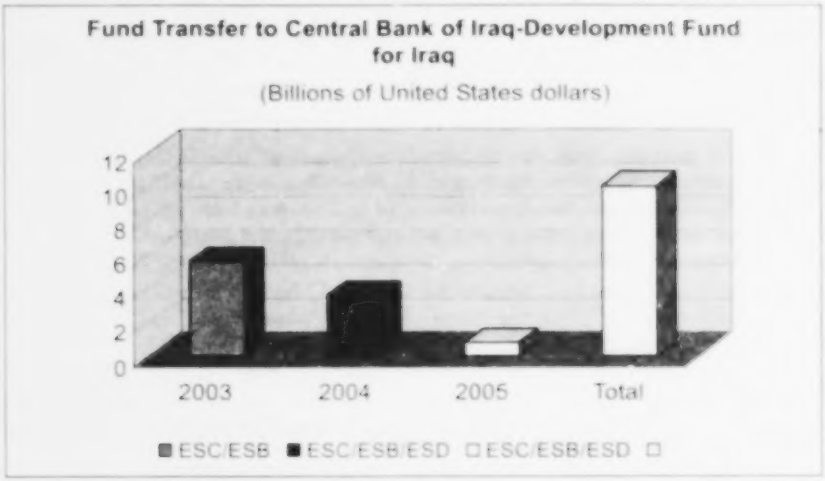


Development Fund for Iraq

14. The Development Fund for Iraq, to be held by the Central Bank of Iraq, was established pursuant to Security Council resolution 1483 (2003). As shown in figure II below, since the adoption of Security Council resolution 1483 (2003), a total amount of $10.04 billion has been transferred to the Development Fund of Iraq as at

31 December 2005, of which $4.44 billion was transferred during the biennium 2004-2005 and charged against the "Humanitarian activities in Iraq" account ($3.99 billion), Administrative and operational costs ($250 million) and UNMOVIC ($200 million).

Figure II



15. The International Advisory and Monitoring Board for Iraq is an audit oversight body for the Development Fund for Iraq. The principal role of the Board is to help ensure that the Development Fund for Iraq is used in a transparent manner for the benefit of the Iraqi people and export sales of petroleum, petroleum products and natural gas from Iraq are made consistent with prevailing international market best practices. The International Advisory and Monitoring Board for Iraq is composed of duly qualified representatives of the Secretary-General, of the Director-General of the Arab Fund for Social and Economic Development, of the Managing Director of the International Monetary Fund and of the President of the World Bank.

B. Detailed findings and recommendations

1. Financial position

16. As reflected in statements I and II, the comparative figures of the major accounts of the United Nations Escrow Fund are presented in table 1.

Table 1
Analysis of account balances
(Thousands of United States dollars)

Account	Biennium ended 2005	Biennium ended 2003	Increase/ decrease	Percentage
Total income	255 759	13 449 195	(13 193 436)	(98)
Total expenditures	421 492	13 163 286	(12 741 794)	(97)
Interest income	166 805	999 427	(832 622)	(83)
Humanitarian supplies and oil spares	279 745	12 405 986	(12 126 241)	(98)
Cash term and deposit	1 389 722	9 571 648	(8 181 926)	(85)
Cash pool	171 529	1 440 971	(1 269 442)	(88)
Unliquidated obligations	1 279 729	7 772 071	(6 492 342)	(84)
Reserves and fund balances	277 265	3 265 376	(2 988 111)	(92)

17. Total income significantly decreased by 98 per cent from 2003 to 2005. The bulk of income in 2003 came from the sale of Iraqi oil. That proportion was reduced owing primarily to the stoppage of oil sales on 20 March 2003. The closure of the programme and the transfer of funds to the Development Fund for Iraq during the biennium 2004-2005 had drastically reduced the funds of the programme. The cash pool, which is the major source of interest income for Iraq accounts, has dropped by $1.27 billion, or 88 per cent, from its balance of $1.44 billion in the biennium ended 2003 to $0.17 billion in the biennium ended 2005. Correspondingly, interest income (in thousands of United States dollars) had decreased from $999,427 in the biennium ended 2003 to $166,805 at the end of the biennium in 2005.

18. Expenditures for the humanitarian supplies and oil spares were $12.40 billion in 2003 and $280 million only in 2005, or a significant decrease of $12.12 billion due to the termination of the programme in November 2003.

19. As at 31 December 2005, cash and term deposits and the cash pool amounted to $1.56 billion. They adequately covered the $1.28 billion unliquidated obligations arising from approved contracts for current and prior periods. The total reserves and fund balances decreased considerably by $2.99 billion from $3.27 billion in 2003 to $277 million in 2005. The decrease is attributed to the fund transfers made to the Development Fund for Iraq.

Liquidation

20. The 2.2 per cent operational and administrative liquidation budget for 2005-2007 amounted to $23.20 million, consisting of $20.84 million for non-staff costs and $2.36 million for staff costs. The non-staff costs of $20.84 million included personnel repatriation costs of $.29 million, building rental costs of $1.74 million, Independent Inquiry Committee investigation costs of $18.31 million, and external audit costs of $.50 million. The Office of Programme Planning, Budget and Accounts assumed the responsibility of completing the winding-up process, including the liquidation of advances by or reimbursement of expenditures to the implementing partners after the termination of the Oil-for-Food Programme on 21 November 2003. As at 31 December 2005, the outstanding advances to the Food and Agriculture Organization of the United Nations of $5 million (including accrued

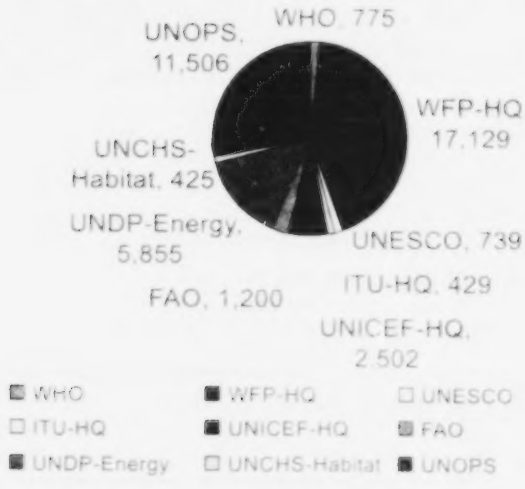
interest of $68,000) involved claim disputes with a third party and disclosed in note 11 to the financial statements as contingent liability.

21. Transactions for the year also included $40.56 million representing overpayment of certain implementation costs, which were billed and subsequently paid by the agencies listed below as a result of the Independent Inquiry Committee findings into the United Nations Oil-for-Food Programme. That amount formed part of the miscellaneous income of the Oil-for-Food Programme.

Figure III

Inter-agency refund to Escrow as a result of the Independent Inquiry Committee report

(Thousands of United States dollars)



22. Transfer of funds to other United Nations agencies charged from the reserves of the UNMOVIC escrow account amounting to $22.71 million was made as at 31 December 2005. Letters from the President of the Security Council dated 24 June 2005 (S/2005/407) and 9 November 2005 (S/2005/703) authorized the transfer of the amount of $20.257 million to the United Nations credited against the assessment issued in respect of the obligations of the Government of Iraq for the regular budget, peacekeeping and Tribunal activities and the Capital Master Plan of the Organization and $2.182 million plus €226,493 for the International Atomic Energy Commission shown in table 2 below.

Table 2

Fund transfers to the United Nations agencies

(Thousands of United States dollars)

United Nations agency	Amount
Regular budget	13 279
Peacekeeping operations	6 228
International Tribunal for the former Yugoslavia	400
International Criminal Tribunal for Rwanda	314
Capital Master Plan	35
International Atomic Energy Agency	2 456
Total	**22 712**

After-sales service fees

23. Security Council resolution 1483 (2003), paragraph 16, provided that the United Nations (Office of the Iraq Programme and the agencies), in coordination with the Coalition Provisional Authority and the relevant Iraq authorities should review the relative utility of each contract still in the pipeline and including also those unfunded contracts on an exceptional basis. Upon the termination of the programme, the Office of the Iraq Programme prioritized 3,060 contracts with an approximate value of $6.2 billion. During that prioritization exercise, contracts that had any after-sales service fees were identified by the Coalition Provisional Authority and the relevant authorities and all contracts identified were renegotiated by the agencies (WFP, WHO, UNICEF, UNDP, UNOPS, and others) and were reduced in value. As a result of those amended contracts, the corresponding letters of credit were also amended to reflect the change in value.

2. United Nations system accounting standards

24. The Board assessed the extent to which the financial statements of the United Nations Escrow Accounts for the biennium 2004-2005 ended 31 December 2005 conformed to the United Nations system accounting standards. The review indicated that the presentation of the financial statements was generally consistent with the standards.

3. Accounts and financial reporting

Expired letters of credit

25. As at 31 December 2005, the United Nations Treasury, using the designated bank's liability report, indicated the final number of amended letters of credit at 498 with an aggregate value of approximately $1.3 billion, as shown in table 3 below. Accordingly, the "cash collateral" associated with the letters of credit covering the prioritized contracts remained in the United Nations Iraq Account until the contracted goods were delivered in full and payments made to the suppliers. The validity of the letters of credit issued and outstanding was extended or new letters of credit issued subject to the amended agreements between the suppliers and the Interim Government of Iraq.

Table 3
Bank liability report as at 31 December 2005
(Thousands of United States dollars)

Expiry date	*Number of letters of credit*	*Value*
2002	1	97
2003	4	2 275
2004	208	165 461
2005	118	254 377
2006	160	650 602
2007	7	189 029
Total	**498**	**1 261 841**

26. The update made by the Secretary-General in his letter dated 19 December 2005, addressed to the President of the Security Council, indicated that the concerned authorities of the Government of Iraq provided the United Nations with 104 requests for amendment and reinstatement to the existing letters of credit, as a result of which shipment dates and validity dates were extended for certain letters of credit. After processing all amendment requests from the relevant government authorities, funding for the 498 letters of credit was retained in the United Nations Iraq account. The validity of the covering letters of credit of the above-mentioned contracts would be allowed to expire but the decision to terminate those contracts would be held in abeyance until after an internationally recognized representative of the Government of Iraq shall make its own determination as to the necessity of enforcing such contracts, pursuant to Security Council resolution 1483 (2003). By May 2006, the United Nations Treasury did not have any documentation to suggest that the Government of Iraq intended to terminate those contracts. The cancellation of expired letters of credit was continuously undertaken by the United Nations Treasury and reflected a declining trend as at 31 March 2006, as shown in table 4.

Table 4
Status of letters of credit for the humanitarian supplies and oil spares

Expiration period	*31 July 2005*	*As reported in the letter of 19 December 2005*	*31 December 2005*	*31 March 2006*
2004	249	223	213[a]	100
2005	286	162	118	83
2006	12	137	160	242
2007	2	2	7	7
Total	**549**	**524**	**498**	**432**

[a] Includes 1 letter of credit originally expiring in December 2002, 2 letters of credit in September 2003 and 2 in December 2003.

27. Of the 498 letters of credit, 331, with an aggregate amount of $422.2 million, had expired as at 31 December 2005 (see table 5 below). Of the 331 letters of credit, 314 had no pending requests for extension. As the liability under a letter of credit automatically ceases to exist upon its expiration, the lack of extension should qualify them for outright cancellation.

Table 5
Expired letters of credit as at 31 December 2005
(Thousands of United States dollars)

Expiry year	*Number of letters of credit*	*Value*
2002	1	97
2003	4	2 275
2004	208	165 461
2005	118	254 377
Total	**331**	**422 210**

28. The non-cancellation of the expired letters of credit hampers the complete liquidation of the programme and holds up cash collaterals associated with each expired letter of credit.

29. The Administration explained that management of the letters of credit programme has been characterized at all stages by a high degree of uncertainty with regard to the validity of the related contracts, letters of credit and obligations. The experience of the Administration has shown that formal expiration dates are not good indicators of intentions to complete contracts within a specified period. The authorities in Iraq have requested extensions of expired letters of credit on multiple occasions, even months after the deadline of receipt of extensions. Accordingly, it would not be prudent to cancel the related unliquidated obligations and to return funds to the Development Fund for Iraq until a clear confirmation was received from the authorities in Iraq that no further requests for extensions would be forwarded.

30. The Security Council extended the validity and/or reinstatement and cancellation of those letters of credit, originally numbering 549 as at 31 July 2005 to 432 as at 31 March 2006. The members of the Security Council also took note of the timetable envisaged in the annex to the Secretary-General's letters of 17 October 2005 and 19 December 2005 that the extension of letters of credit were to be received by the United Nations Treasury up to 31 December 2005.

31. **The Board recommends that the Administration:**

(a) strongly urge the Security Council and the Government of Iraq to finally resolve the issue of contracts with expired letters of credit; and

(b) continue to coordinate closely with the designated bank for the release of the cash collateral associated with each expired letter of credit in order to adjust the unliquidated obligations at the time the cash collateral is released by the bank.

32. The Administration informed the Board that the Controller is in the process of finalizing a report to be sent by the Secretary-General to the President of the Security Council on the arrangements for terminating the operations relating to the letters of credit raised against the United Nations Iraq Account under Security Council resolution 1483 (2003). The Secretary-General would be sending an update to the President of the Security Council as at 31 May 2006.

Unliquidated obligations

33. The Board noted a variation of $16 million in the balances of unliquidated obligations in the escrow financial statements. The unliquidated obligations as at 31 December 2005 amounted to $1.277 billion, compared to the designated bank-generated report in the amount of $1.261 billion, or a difference of $16 million. The Board noted that the Office of Programme Planning, Budget and Accounts had conducted regular reconciliations of the unliquidated obligations balances among the designated bank's outstanding letters of credit and the miscellaneous obligations documents in IMIS and the United Nations Treasury. The latest reconciliation as at 31 December 2005 was conducted on 16 March 2006. There was a 54 per cent decrease of unreconciled unliquidated obligations balances from $35 million in 2004 to the present $16 million.

34. The difference was due mainly to reinstatements which were not immediately recorded by the designated bank and/or the fact that although the designated bank was authorized to reinstate the full values of the letters of credit as recorded in the books of the Administration, the designated bank reinstated only amounts necessary to pay obligations due to beneficiaries. Another reason was that, in instances where suppliers were charged with penalties for late shipments, the bank paid them net of penalties but the United Nations kept the original amount. Hence, the unliquidated obligations as recorded in IMIS included the penalties.

35. The Board noted the orderly custody of thousands of contracts for humanitarian supplies and oil spares, more particularly their electronic filing. That provided the assurance of the availability and ease of retrieval of supporting documents.

Operating reserves

"Humanitarian activities in Iraq" account

36. An operating reserve of $160 billion was established during the six-month period ended 30 June 2005 under the "humanitarian activities in Iraq" account. The reserve was to ensure that sufficient funds were available for the satisfactory resolution of all remaining issues relating to outstanding letters of credit. With the reduction in the number of outstanding letters of credit, the operating reserve was reduced to $126.7 billion as at 31 December 2005.

"Administrative and operational costs" account

37. An operating reserve of $48 million was established in 2004 under the "administrative and operational costs" account. The reserve was to meet compensation costs payable in respect of those Oil-for-Food Programme staff members who were injured or killed as a result of the bombing of the United Nations headquarters building in Baghdad on 19 August 2003, as well as the

expected costs of the Independent Inquiry Committee and the administrative costs of the Escrow Accounts until all aspects of the programme are completed.

38. During the period from 1 January to 31 December 2005, an amount of $37.2 million was disbursed to meet those costs, which consisted mainly of Independent Inquiry Committee costs of $23.9 million and full settlement of all costs related to the bombing of 19 August 2003. An additional reserve was established for $10.4 million that included Independent Inquiry Committee costs of $6.6 million, thereby resulting in an operating reserve of $21.1 million as at 31 December 2005. That reserve is to meet future costs chargeable to the "administrative and operational costs" account, including those relating to Independent Inquiry Committee and administrative costs.

4. Liabilities for end-of-service benefits

39. Staff members separated from the Organization were entitled to be paid for any unused vacation days that they may have accrued, up to a maximum of 60 days. The Organization's total liability for such unpaid accrued vacation compensation for staff working in the various activities related to Security Council resolutions 687 (1991), 706 (1991), 778 (1992), 986 (1995), 1284 (1999), and 1483 (2003) as of 31 December 2005 was estimated at $1.1 million.

40. Some staff members are entitled to repatriation grants and related expenditures of relocation upon their separation from the Organization based on the number of years of service. The Organization's total liability for such unpaid repatriation and relocation entitlement for staff working in the various activities related to the above-mentioned Security Council resolutions as of 31 December 2005 was estimated at $0.9 million. The Board noted that the operating reserves of $21 million established in 2005 included provisions for those liabilities.

5. Write-off of losses

41. In accordance with financial rule 106.8 (a), the Administration also provided the Board a schedule of cash and receivables written off during the biennium ended 31 December 2005. A total of $4,358 for receivables pertaining to the United Nations Escrow Account was written off. The amount consisted mainly of losses of unsold United Nations stamps of $3,540.

6. Ex gratia payments

42. In accordance with financial rule 105.12, the Administration informed the Board that there were ex gratia payments amounting to $214,151 during the biennium ended 31 December 2005. The payments consisted of medical expenses of four staff, two United Nations visitors and two workers who were injured during the bombing of the United Nations office in Baghdad in 2003.

7. United Nations Monitoring, Verification and Inspection Commission

UNMOVIC mandate

43. In paragraph 22 of its resolution 1546 (2004), the Security Council reaffirms its intention to revisit the mandates of UNMOVIC and the International Atomic Energy Agency (IAEA). The UNMOVIC assets as at 31 December 2005 included

$115 million in the cash pool. That represents the share in the United Nations Headquarters cash pool for UNMOVIC, comprising cash and term deposits of $17.89 million, short-term investments of $52.33 million, long-term investments of $43.83 million and accrued interest receivable of $0.72 million. The UNMOVIC assets on the cash pool represents 67 per cent of the total cash pool of the escrow account of $171.53 million. UNMOVIC had approximately $114 million total reserves and fund balances as at 31 December 2005, down from $353 million as at 31 December 2003. A total of $32 million administrative expenses were incurred for the biennium ended 31 December 2005, compared to $73 million for the biennium ended 31 December 2003. Also, an amount of $200 million was transferred to the Development Fund for Iraq and $22.7 million was used to settle the outstanding arrears of assessed contributions that the Government of Iraq had with the United Nations and the IAEA. The staffing table authorization dated 28 June 2005 indicated 67 positions for Professional and General Services.

44. In the report of the Secretary-General on mandating and delivering: analysis and recommendations to facilitate the review of mandates (A/60/733 and Corr.1), the Secretary-General indicated that as the "situation in Iraq evolves, a Security Council review of the UNMOVIC mandate may be warranted, including examination of whether and how the United Nations could utilize certain areas of the Commission's expertise such as its roster of trained technical experts".

45. Although the operational activities of UNMOVIC have diminished, administrative expenses still amounted to $32 million while the balance of reserves as at 31 December 2005 was $114 million. Without its mandates being revisited as required in resolutions 1483 (2003) and 1546 (2004), UNMOVIC may continue to incur administrative costs although most of its goals and objectives may have been overtaken by events.

46. **The Board recommends that the Administration initiate the evaluation of the UNMOVIC mandate in the light of current events and again invite the Security Council to steer the final course of action to be taken.**

47. The Administration has, however, pointed out in that connection that it regularly kept the Security Council informed of its programme activities. The Council has also been informed of the level of the reserve and of the possibility of reviewing the mandate.

Deferred payable

48. The other accounts payable of UNMOVIC funds or Fund ESE has a balance of $751 million. Of that amount, $579,268 represented deferred payable to the Government of Germany for the helicopter flights provided to UNSCOM (now UNMOVIC) in the early 1990s. The Administration commented that Office of Programme Planning, Budget and Accounts has reviewed the situation once again with UNMOVIC. It concluded that appropriate action should be taken once the Security Council has decided on the future mandate of UNMOVIC. The same observation was raised in the audit report of the escrow account for the financial period ended 31 December 2004.

Non-expendable property

49. The Board noted that the value of property lost and stolen during the bombing of the headquarters on 19 August 2003 and the reported lootings on 18 November 2003 and 23 August 2004 were not determined and identified. The notes to the financial statements disclosed that owing to the situation in Iraq, it was not possible for UNMOVIC to ascertain the value of non-expendable property in Iraq as at 31 December 2005.

50. The Administration informed the Board that all UNMOVIC assets at the Canal compound in Baghdad have been repositioned in a programme which involved the presence in Iraq of two UNMOVIC international staff. UNMOVIC equipment was stored in three locations, namely, the International Zone in Baghdad, the United Nations compound in Kuwait, and the UNMOVIC Cyprus field office. UNMOVIC international staff has commenced the final inventory of non-expendable property that would be completed by the end of August 2006.

51. **The Board recommends that UNMOVIC facilitate completion of the final inventory necessary to update its records of non-expendable property lost or stolen.**

8. Action taken by the Administration on the findings of the Independent Inquiry Committee

52. The Independent Inquiry Committee issued its fifth and final substantive report on 27 October 2005 on the alleged manipulation of the Oil-for-Food Programme. The report stated that the former Iraq Government had manipulated the programme to dispense contracts on the basis of political preference and to derive illicit payments from companies that obtained oil and humanitarian goods contracts. Four interim reports were issued and published by the Independent Inquiry Committee:

(a) Interim report dated 3 February 2005 dealing with the "initial procurement of United Nations contractors', Benon Sevan and oil allocation, internal programme audits and management of the programme's administrative account";

(b) Second interim report dated 29 March 2005 covering the "1998 procurement of the humanitarian goods inspection contract and other conduct of United Nations officials";

(c) Third interim report dated 8 August 2005 covering "the conduct of Benon Sevan and the conduct of Alexander Yakovlev"; and

(d) Report on the "management of the Oil-for-Food Programme dated 7 September 2005".

53. The work of the Independent Inquiry Committee was substantially completed during the year ended 31 December 2005. The Office of the Independent Inquiry Committee was officially disbanded in December 2005. However, the Committee's term was extended through 31 December 2006 to assist duly authorized law enforcement and regulatory agencies in cases that these agencies may be pursuing against companies, individuals and other entities resulting from the Committee's work. The Committee members have agreed to continue as an "Advisory Panel" on policy and operational issues that may arise. Costs of the Committee are paid for

from funds for administrative and operational costs of the programme. Expenditures during the 3- annum 2004-2005 ending 31 December 2005 amounted to approximately $36 million, of which $12 million pertained to 2004 and $23.4 million to 2005.

54. The plan of corrective action by the Office of Programme Planning, Budget and Accounts took into account the findings, conclusions and recommendations of the Independent Inquiry Committee as contained in the five reports which the Committee has issued. However, the Independent Inquiry Committee identified a number of positive findings related to controls and procedures in Office of Programme Planning, Budget and Accounts, inter alia, in the areas of management of the ESD (Programme Administrative Expenditure) Account and Treasury Operations. The Independent Inquiry Committee also drew attention to the fact that the procurement process was strongly tested by the need to quickly implement an urgent, complex and unprecedented programme.

55. The Administration also billed various United Nations agencies for the overpayment of certain implementation costs aggregating $40.56 million as a result of the Independent Inquiry Committee report. The concerned United Nations agencies paid the overpayment and the amount formed part of the miscellaneous income of the Oil-for-Food Programme (see para. 21 above).

56. The forensic investigation conducted in the aftermath of the Independent Inquiry Committee investigation has not yet been concluded, in view of which no impact on the financial statements was not yet known.

9. Cases of fraud and presumptive fraud

57. Notwithstanding the investigation by the Independent Inquiry Committee and any ongoing investigations by law enforcement officers of Member States, the Administration advised the Board that there were no known cases of fraud or presumptive fraud in the processing activities of the programme, nor in the operations of UNMOVIC, during the period under audit.

C. Acknowledgment

58. The Board wishes to express its appreciation for the cooperation and assistance extended to the auditors by the Secretary-General, the Under-Secretary-General for Management, the Acting Executive Chairman, United Nations Monitoring, Verification and Inspection Commission and their officers and staff.

(Signed) Guillermo N. **Carague**
Chairman, Commission on Audit, Republic of the Philippines
Chairman, United Nations Board of Auditors
(Lead Auditor)

(Signed) Shauket A. **Fakie**
Auditor-General of the Republic of South Africa

(Signed) Philippe **Seguin**
First President of the Court of Accounts of France

31 July 2006

Annex

Summary of status of implementation of recommendations for the financial period ended 31 December 2003

No.	Recommendation	Reference	Year first recommended	Status	Reference to paragraphs in present report
1	Transfer of expenditure from the Trust Fund for Peacekeeping Contingency Operations and Other Purposes to the Trust Fund for Peacekeeping Operations and the Trust Fund for Humanitarian Assistance, Relief and Rehabilitation	Table 2.1	Paragraph 39, Board's report 2002		Paragraphs 23-25
2	Enhance the accounting of contributions in the Mission Subaccount to reflect the receipt of contributions on the scheduled payment dates	Table 2.1	Paragraph 41, Board's report 2002		Paragraphs 23-25
Total			2	2	

II. Audit opinion

We have audited the accompanying financial statements of the United Nations Escrow (Iraq) Account comprising statements I to III and the supporting notes to the financial statements for the biennium ended 31 December 2005. These financial statements are the responsibility of the Secretary-General of the United Nations. Our responsibility is to express an opinion on the financial statements based on our audit and taking into account our opinion expressed on the financial statements for the period 1 January to 31 December 2004.

We conducted our audit in accordance with the common auditing standards of the Panel of External Auditors of the United Nations, the specialized agencies and the International Atomic Energy Agency and the International Standards on Auditing. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the Secretary-General, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for the audit opinion.

In our opinion, the financial statements present fairly, in all material respects, the financial position as at 31 December 2005 and the results of its operations and its cash flows for the biennium then ended, in accordance with the United Nations system accounting standards.

Furthermore, in our opinion, the transactions of the United Nations Escrow (Iraq) Account that have come to our notice, or which we have tested as part of our audit, have in all significant respects been in accordance with the Financial Regulations and legislative authority.

Without qualifying our audit opinions expressed above, we draw attention to note 12 to the financial statements, relative to the results of the investigation conducted by the Independent Inquiry Committee that was completed and its final report issued on 27 October 2005. The Administration noted the findings and was in the process of taking appropriate action on the recommendations of the Independent Inquiry Committee.

(*Signed*) Guillermo N. **Carague**
Chairman, Commission on Audit, Republic of the Philippines
(Chairman, United Nations Board of Auditors)
(Lead Auditor)

(*Signed*) Shauket A. **Fakie**
Auditor-General of the Republic of South Africa

(*Signed*) Philippe **Seguin**
First President of the Court of Accounts of France

28 July 2006

Certification of the financial statements

1. The financial statements pursuant to Security Council resolution 986 (1995), and pursuant to Security Council resolutions 687 (1991), 706 (1991), 778 (1992), 1284 (1999), 1483 (2003) and 1546 (2004), for the period 1 January 2004 to 31 December 2005 have been prepared in accordance with financial rule 106.10.

2. The summary of significant accounting policies applied in the preparation of these statements is included as notes to the financial statements. These notes provide additional information and clarifications for the financial activities related to Security Council resolutions 687 (1991), 706 (1991), 778 (1992), 986 (1995), 1284 (1999), 1483 (2003) and 1546 (2004) undertaken by the Organization during the period covered by these statements, for which the Secretary-General has administrative responsibility.

3. I certify that the appended financial statements of the United Nations Escrow Accounts, numbered I to III, are correct.

(*Signed*) Warren **Sach**
Assistant Secretary-General
Controller

31 March 2006

Statement I

United Nations Escrow Accounts established under the provisions of Security Council resolutions relating to Iraq a/

Statement of income and expenditures and changes in reserves and fund balances
for the biennium 2004–2005 ending 31 December 2005

(Thousands of United States dollars)

	Security Council resolutions 986 (1995) and 1483 (2003)		Security Council resolutions 687 (1991), 706 (1991), 1284 (1999) c/	Security Council resolutions 687 (1991), 706 (1991) d/		
	Humanitarian activities in Iraq b/	**Administrative and operational costs**	**Monitoring, verification and inspection**	**Other activities**	**Total 2005**	**Total 2003**
Income						
Sale of Iraqi oil						13 548 112
Allocation to United Nations Compensation Commission						(3 423 852)
Subtotal	–	–	–	–	–	**10 124 260**
Funding from operating reserves e/		37 242			37 242	
Interest income	150 096	3 329	13 380		166 805	999 427
Miscellaneous income	43 365 f/	8 148	192		51 705	6 976
Currency exchange adjustments g/		6	1		7	2 318 532
Total income	**193 461**	**50 725**	**11 573**	–	**255 759**	**13 449 195**
Expenditure						
Purchase of humanitarian supplies h/	280 358				280 358	11 139 750
Purchase of spare parts i/	79 387				79 387	1 286 216
Pipeline tariff charges						289 714
Operational expenses by Inter-Agencies		2 496			2 496	236 652
Administrative expenses		27 712 j/	31 723	484	59 919	215 225
Independent Inquiry Committee expenses k/		35 854			35 854	
Interest expense						15 709
Currency exchange adjustments g/	43 478				43 478	
Total expenditure	**323 223**	**66 062**	**31 723**	**484**	**421 492**	**13 163 286**
Excess (shortfall) of income over expenditure	(129 762)	(15 337)	(20 150)	(484)	(165 733)	285 909

	Security Council resolutions 986 (1995) and 1483 (2003)		Security Council resolutions 687 (1991), 706 (1991), 1284 (1999), g	Security Council resolutions 687 (1991), 706 (1991), g		
	Humanitarian activities in Iraq b	Administrative and operational costs	Monitoring, verification and inspection	Other activities	Total 2005	Total 2003
Prior-period adjustments		(1)		(4)	(5)	
Net excess (shortfall) of income over expenditure	(129 762)	(15 338)	(20 156)	(488)	(165 738)	285 908
Savings on/or cancellation of prior-period obligations	1 642 507	31 450	3 694	252	1 677 903	1 332 254
Other adjustments to fund balances						4
Transfers (to) from other organizations k	(3 990 322)	(250 000)	(200 000)		(4 440 322)	(5 000 000)
Transfers to the United Nations and IAEA m			(22 712)		(22 712)	
Transfer from operating reserves e		(37 242)			(37 242)	
Reserves and fund balances, beginning of period	2 613 358	298 303	353 096	619	3 265 376	5 247 209
Reserves and fund balances, end of period	**135 781**	**27 173**	**113 928**	**383**	**277 265**	**3 265 376**

a/ There were no activities relating to pipelines tariff charges and assets transfers and contributions during this period. Also see notes 3 and 4.

b/ Based on Security Council resolution 1483 (2003) amounts previously shown separately in respect of the "15 Governorates of Central and Southern Iraq", and "3 Governorates of Northern Iraq" have been combined under "Humanitarian activities in Iraq".

c/ Refers to the United Nations Monitoring Verification and Inspection Commission, see note 4.

d/ Refers to activities undertaken further to Security Council resolutions 687 (1991) and 706 (1991), see note 4.

e/ See note 7.

f/ Includes reimbursable implementation costs of $40,560,579 from agencies. See note 6.

g/ Represents currency exchange fluctuations between the euro and the United States dollar and other currencies.

h/ Expenditure incurred during the 2004-2005 biennium for humanitarian supplies relates to adjustments and reinstatements of contracts entered into in previous years. The figure includes unliquidated obligations of $75,291,447.

i/ Expenditure incurred during the 2004-2005 biennium for spare parts relates to adjustments and reinstatements of contracts entered into in previous years. The figure includes unliquidated obligations of $28,123,359.

j/ Includes $10,000,000 transferred to the Special Account for Compensation Awards and After-Service Health Insurance Payments (that is accounted for in volume I of the United Nations), in order to provide for medical and related costs arising from the 19 August 2003 bombing in Baghdad, Iraq.

k/ See note 5.

l/ Represents transfers to the Development Fund for Iraq held by the Central Bank of Iraq pursuant to Security Council resolution 1483 (2003). See note 10 (e).

m/ Represents transfers of $20,256,697 to the United Nations, and $2,182,168 plus €226,493 to the International Atomic Energy Agency for payment of outstanding assessed contributions of the Government of Iraq pursuant to the letters dated 24 June 2005 (S/2005/407) and 9 November 2005 (S/2005/703) from the President of the Security Council.

The accompanying notes are an integral part of the financial statements.

Statement II

United Nations Escrow Accounts established under the provisions of Security Council resolutions relating to Iraq a/

Statement of assets, liabilities and reserves and fund balances
as at 31 December 2005

(Thousands of United States dollars)

	Security Council resolutions 986 (1995) and 1483 (2003)		Security Council resolutions 687 (1991), 706 (1991), 1284 (1999)	Security Council resolutions 687 (1991), 706 (1991)		
	Humanitarian activities in Iraq	**Administrative and operational costs**	**Monitoring, verification and inspection**	**Other activities**	**Total 2005**	**Total 2003**
Assets						
Cash and term deposits	1 389 649	43	30	-	1 389 722	9 571 648
Cash pool	17 154 b	39 610 c	114 765 d		171 529	1 440 971
Accounts receivable						
Inter-fund balances receivable e				367	367	2 677
Accounts receivable from Inter-Agencies f	4 836	121	355	-	5 312	70 580
Other accounts receivable	2 074	203	411	28	2 716	11 373
Inter-office transactions pending processing	-	-	-	-	-	264
Deferred charges	-	15	25	-	40	3 249
Total assets	**1 413 713**	**39 992**	**115 586**	**395**	**1 569 686**	**11 100 762**
Liabilities						
Unliquidated obligations - current year	103 739 g	1 658	350	3	105 750	6 788 095
Unliquidated obligations - prior years	1 173 979	-	-	-	1 173 979	980 795
Unliquidated obligations - future years	-	-	-	-	-	3 181
Accounts payable						
Inter-fund balances payable e	214	10 847	467	-	11 528	5 751
Accounts payable to Inter-Agencies h	-	-	90	-	90	52 887
Other accounts payable	-	313	751	9	1 073	4 592
Inter-office transactions pending processing	-	1	-	-	1	85
Total liabilities	**1 277 932**	**12 819**	**1 658**	**12**	**1 292 421**	**7 835 386**
Reserves and fund balances						
Operating reserves i	126 660	21 132	-	-	147 792	-
Cumulative surplus	9 121	6 041	113 928	383	129 473	3 265 376
Total reserves and fund balances	**135 781**	**27 173**	**113 928**	**383**	**277 265**	**3 265 376**
Total liabilities and reserves and fund balances	**1 413 713**	**39 992**	**115 586**	**395**	**1 569 686**	**11 100 762**

a There were no activities relating to pipelines tariff charges and assets transfers and contributions during this period. Also see notes 3 and 4.

b Represents share of United Nations Headquarters cash pool for the "humanitarian activities in Iraq" comprising cash and term deposits $2,672,884, short-term investments $7,822,080 (market value $7,822,080), long-term investments $6,851,825 (market value $6,467,456), accrued interest receivable $107,017.

c Represents share of the United Nations Headquarters cash pool for "administrative and operational costs" cash and term deposits $6,172,011, short-term investments $18,062,122 (market value $18,062,122), long-term investments $15,128,951 (market value $14,934,131), accrued interest receivable $247,114.

d Represents share of the United Nations Headquarters cash pool for "monitoring, verification and inspection" cash and term deposits $17,882,625, short-term investments $52,332,726 (market value $52,332,726) long-term investments $43,834,234 (market value $43,269,768) and accrued interest receivable $715,982.

e See note 2 k (iv).

f Includes reimbursable implementation costs and funds advanced for the implementation of humanitarian activities.

g Unliquidated obligation incurred during the 2004-2005 biennium for humanitarian supplies and spare parts relates to adjustments and reinstatements of contracts entered into in previous years.

h Represents amounts payable to United Nations Inter-Agencies for expenditures in excess of amounts advanced.

i See note 7.

The accompanying notes are an integral part of the financial statements.

Statement III

United Nations Escrow Accounts established under the provisions of Security Council resolutions relating to Iraq a

Statement of cash flows
for the biennium 2004-2005 ending 31 December 2005

(Thousands of United States dollars)

	Security Council resolutions 986 (1995) and 1483 (2003)		Security Council resolutions 687 (1991), 706 (1991), 1284 (1999)	Security Council resolutions 687 (1991), 706 (1991)		
	Humanitarian activities in Iraq	Administrative and operational costs	Monitoring, verification and inspection	Other activities	Total 2005	Total 2003
Cash flows from operating activities						
Net excess (shortfall) of income over expenditure (Statement II)	(129 762)	(15 318)	(20 350)	(388)	(165 718)	285 909
(Increase) decrease in accounts receivable from sales of Iraqi oil						645 070
(Increase) decrease in inter-fund balances receivable	1 810			500	2 310	37 181 b
(Increase) decrease in accounts receivable from Inter-Agencies	61 983	2 237	1 048		65 268	(5 632)
(Increase) decrease in other accounts receivable	7 869	400	310	(36)	8 637	117 618
(Increase) decrease in other assets		264			264	(152)
(Increase) decrease in deferred charges		2 871	638		3 209	3 205
Increase (decrease) in unliquidated obligations	(6 435 811)	(51 444)	(4 837)	(250)	(6 492 342)	(5 431 239)
Increase (decrease) in frozen assets transfers and contributions payable						(308 404)
Increase (decrease) in inter-fund accounts payable	214	6 750	(1 187)		5 777	(246 724) b
Increase (decrease) in accounts payable to Inter-Agencies	(37 269)	(15 334)	(194)		(52 797)	35 933
Increase (decrease) in other accounts payable	(2 796)	(719)	(8)	4	(3 519)	(1 251)
Increase (decrease) in accrued interest payable						(137 906)
Increase (decrease) in other liabilities		(84)			(84)	–
Less: Interest income	(150 096)	(5 329)	(11 380)	–	(166 805)	(999 427)
Net cash from operating activities	**(6 683 858)**	**(75 930)**	**(35 760)**	**(252)**	**(6 795 800)**	**(6 027 610)**
Cash flows from investing activities						
(Increase) decrease in cash pool	701 336	324 000	243 207	–	1 269 442	8 251 575
Plus: Interest income	150 096	5 329	11 380		166 805	999 427
Net cash from investing activities	**851 432**	**330 228**	**254 587**	**–**	**1 436 247**	**9 251 002**
Cash flows from financing activities						
Savings on, or cancellation of prior-period obligations	1 642 507	31 450	1 694	252	1 675 903	1 332 254
Other adjustments to fund balances						4
Transfers (to) from other organizations	(3 990 322)	(250 000)	(260 000)		(4 440 322)	(5 600 000)
Transfers to the United Nations and IAEA		–	(22 712)		(22 712)	–
Transfer from operating reserves		(37 242)			(37 242)	–
Net cash from financing activities	**(2 347 815)**	**(255 792)**	**(219 018)**	**252**	**(2 822 373)**	**(2 267 742)**
Net increase (decrease) in cash and term deposits	(9 180 241)	(1 494)	(191)	–	(8 181 926)	955 650
Cash and term deposits, beginning of period	**9 569 890**	**1 537**	**221**	**–**	**9 571 648**	**8 615 998**
Cash and term deposits, end of period	**1 389 649**	**43**	**30**	**–**	**1 389 722**	**9 571 648**

a. There were no activities relating to pipelines tariff charges and assets transfers and contributions during this period. Also see notes 3 and 4.
b. Reclassified to conform to current presentation.

The accompanying notes are an integral part of the financial statements.

Notes to the financial statements for the United Nations Escrow Account established under the provisions of Security Council resolutions relating to Iraq

Note 1
The United Nations and its activities

(a) The Charter of the United Nations was signed on 26 June 1945 and came into force on 24 October 1945. The Organization's primary objectives, to be implemented through its five major organs, are as follows:

(i) The maintenance of international peace and security;

(ii) The promotion of international economic, social progress and development programmes;

(iii) The universal observance of human rights;

(iv) The administration of international justice and law;

(v) The development of self-government for Trust Territories;

(b) The General Assembly focuses on a wide range of political, economic and social issues as well as the financial and administrative aspects of the Organization;

(c) Under the direction of the Security Council, the Organization has been involved in various aspects of peacekeeping and peacemaking, including efforts to resolve conflicts, restore democracy, promote disarmament, provide electoral assistance, facilitate post-conflict peacebuilding, engage in humanitarian activities to ensure survival of groups deprived of basic needs and overseeing the prosecution of persons responsible for serious violations of international humanitarian law;

(d) The Economic and Social Council plays a particular role in economic and social development, including a major oversight role in the efforts of other organizations of the United Nations system to address international economic, social and health problems;

(e) The International Court of Justice has jurisdiction over disputes between Member States brought before it for advisory opinions or binding resolutions;

(f) The Trusteeship Council completed its primary functions in 1994 with the termination of the Trusteeship Agreement for the last United Nations Trust Territory.

Note 2
Summary of significant accounting and financial reporting policies of the United Nations

(a) The accounts of the United Nations are maintained in accordance with the Financial Regulations and Rules of the United Nations as adopted by the General Assembly, the rules formulated by the Secretary-General as required under the regulations and administrative instructions issued by the Under-Secretary-General for Management or the Controller. They also take fully into account the United Nations system accounting standards, as adopted by the Administrative Committee on Coordination, which has since been replaced by the United Nations

System Chief Executives Board for Coordination. The Organization follows international accounting standard 1, "presentation of financial statements", on the disclosure of accounting policies, as modified and adopted by the United Nations System Chief Executives Board for Coordination as follows:

(i) Going concern, consistency, and accrual are fundamental accounting assumptions. Where fundamental accounting assumptions are followed in financial statements, disclosure of such assumptions is not required. If a fundamental accounting assumption is not followed, that fact should be disclosed together with the reasons;

(ii) Prudence, substance over form and materiality should govern the selection and application of accounting policies;

(iii) Financial statements should include clear and concise disclosure of all significant accounting policies that have been used;

(iv) The disclosure of the significant accounting policies used should be an integral part of the financial statements. These policies should normally be disclosed in one place;

(v) Financial statements should show comparative figures for the corresponding period of the preceding financial period;

(vi) A change in an accounting policy that has a material effect in the current period or may have a material effect in subsequent periods should be disclosed together with the reasons. The effect of the change should, if material, be disclosed and quantified;

(b) The Organization's accounts are maintained on a fund accounting basis. Separate funds for general or special purposes may be established by the General Assembly, the Security Council or the Secretary-General. Each fund is maintained as a distinct financial and accounting entity with a separate self-balancing double-entry group of accounts. Separate financial statements are prepared for each fund or for a group of funds of the same nature;

(c) The financial period of the Organization is a biennium and consists of two consecutive calendar years for all funds other than peacekeeping accounts, which are reported on a fiscal year basis covering the period from 1 July to 30 June;

(d) Generally, income, expenditure, assets, and liabilities are recognized on the accrual basis of accounting;

(e) The accounts of the Organization are presented in United States dollars. Accounts maintained in other currencies are translated into United States dollars at the time of the transactions at rates of exchange established by the United Nations. In respect of such currencies, the financial statements shall reflect the cash, investments, unpaid pledges and current accounts receivable and payable in currencies other than the United States dollars translated at the applicable United Nations rates of exchange in effect as at the date of the statements. In the event that the application of actual exchange rates at the date of the statements would provide a valuation materially different from the application of the Organization's rates of exchange for the last month of the financial period, a footnote will be provided quantifying the difference;

(f) The Organization's financial statements are prepared on the historical cost basis of accounting and are not adjusted to reflect the effects of changing prices for goods and services;

(g) The cash flow summary statement is based on the indirect method of cash flows, as referred to in the United Nations system accounting standards;

(h) The Organization's financial statements are presented in accordance with the ongoing recommendations of the Task Force on Accounting Standards to the United Nations System Chief Executives Board for Coordination;

(i) Income

(i) Voluntary contributions from Member States or other donors are recorded as income on the basis of a written commitment to pay monetary contributions at specified times within the current financial period. Voluntary contributions made in the form of services and supplies that are acceptable to the Secretary-General are credited to income or noted in the financial statements;

(ii) Income received under inter-organizational arrangements represents allocations of funding from agencies to enable the Organization to administer projects or other programmes on their behalf;

(iii) Allocations from other funds represent monies appropriated or designated from one fund for transfer to and disbursement from another fund;

(iv) Income for services rendered includes amounts charged for salaries of staff members and other costs that are attributable to the provision of technical and administrative support to other organizations;

(v) Interest income includes all interest earned on deposits in various bank accounts, investment income earned on marketable securities and other negotiable instruments, and investment income earned on the cash pool. All realized losses and net unrealized losses on short-term investments are offset against investment income. Investment income and costs associated with operation of investments in the cash pool are allocated to participating funds. Interest income is available for allotment purposes on a six-monthly basis;

(vi) Net gains or losses on currency fluctuations other than for current year's obligations are accumulated on a six-monthly basis. Effective 1 January 2002, the net amount is recognized as income or expenditure every six months in the financial statements;

(vii) Miscellaneous income includes income from rental of premises, sale of used or surplus property, refunds of expenditures charged to prior periods, settlements of insurance claims, monies accepted for which no purpose was specified, and other sundry income;

(viii) Income relating to future financial periods is not recognized in the current financial period and is recorded as deferred income as referred to in paragraph (l) (iii) below;

(j) Expenditure

(i) Expenditures are incurred against authorized appropriations or commitment authorities. Total expenditures reported include unliquidated

obligations and disbursements. Expenditures also include currency exchange adjustments arising from evaluation of current-period obligations.

(ii) Expenditures incurred for non-expendable property are charged to the budget of the period when the property is acquired and are not capitalized. Inventory of such non-expendable property is maintained at historical cost.

(iii) Expenditures for future financial periods are not charged to the current financial period and are recorded as deferred charges, as referred to in paragraph (k) (vi) below.

(k) Assets

(i) Cash and term deposits represent funds in demand deposit accounts and interest-bearing bank deposits.

(ii) Investments include marketable securities and other negotiable instruments acquired by the Organization to produce income. Short-term investments are stated at lower of cost or market; long-term investments are stated at cost. Cost is defined as the nominal value plus or minus any unamortized premium or discount. The market value of investments is disclosed in the footnotes to the financial statements.

(iii) Cash pools comprise participating funds' share of the cash and term deposits, short-term and long-term investments and accrual of investment income, all of which are managed in the cash pools. The investments in the cash pools are similar in nature. Short-term investments are stated at lower of cost or market; long-term investments are stated at cost. Cost is defined as the nominal value plus or minus any unamortized premium or discount. The share in cash pools is reported separately in each of the participating fund's statement, and its composition and the market value of its investments are disclosed in footnotes in the individual statements.

(iv) Inter-fund balances reflect transactions between funds, and are included in the amounts due to and from the United Nations General Fund. Inter-fund balances also reflect transactions directly with other escrow accounts and with the United Nations General Fund. Inter-fund balances are settled periodically, dependent upon availability of cash resources.

(v) Provision for delays in collection of receivable balances is not made.

(vi) Deferred charges normally comprise expenditure items that are not properly chargeable in the current financial period. They will be charged as expenditure in a subsequent period. These expenditure items include commitments approved by the Controller for future financial periods in accordance with financial rule 106.7. Such commitments are normally restricted to administrative requirements of a continuing nature and to contracts or legal obligations where long lead times are required for delivery.

(vii) For purposes of the balance sheet statements only, those portions of education grant advances that are assumed to pertain to the scholastic years completed as at the date of the financial statement are shown as deferred charges. The full amounts of the advances are maintained as accounts receivable from staff members until the required proofs of entitlement are

produced, at which time the budgetary accounts charged, and the advances settled;

(viii) Maintenance and repairs of capital assets are charged against the appropriate budgetary accounts. Furniture, equipment, other non-expendable property, and leasehold improvements are not included in the assets of the Organization. Such acquisitions are charged against budgetary accounts in the year of purchase. The value of non-expendable property is disclosed in notes to the financial statements;

(l) Liabilities and reserves and fund balances:

(i) Operating reserves are included in the totals for reserves and fund balances shown in the financial statements;

(ii) Unliquidated obligations for future years are reported both as deferred charges and as unliquidated obligations;

(iii) Deferred income includes income received but not yet earned;

(iv) Commitments of the Organization relating to prior, current and future financial periods are shown as unliquidated obligations. Effective 1 January 2000, unliquidated obligations for the escrow account for humanitarian activities in Iraq remain valid until completion of the project. All other obligations continue to remain valid for 12 months following the end of the biennium to which they relate;

(v) Contingent liabilities, if any, are disclosed in the notes to the financial statements;

(vi) The United Nations is a member organization participating in the United Nations Joint Staff Pension Fund, which was established by the General Assembly to provide retirement, death, disability and related benefits. The Pension Fund is a funded defined benefit plan. The financial obligation of the Organization to the Pension Fund consists of its mandated contribution at the rate established by the General Assembly together with its share of any actuarial deficiency payments under article 26 of the Regulations of the Pension Fund. Such deficiency payments are payable only if and when the General Assembly has invoked the provision of article 26, following determination that there is a requirement for deficiency payments based on an assessment of the actuarial sufficiency of the Pension Fund as at the valuation date. As at the date of the current financial statement, the General Assembly has not invoked this provision.

Note 3
United Nations escrow account established under the provisions of Security Council resolution 986 (1995) (statements I, II and III)

(a) An escrow account to be administered by the Secretary-General was established in 1996 in order to receive the proceeds from sale of Iraqi oil as approved by Security Council resolution 986 (1995). The Security Council, in paragraph 1 of resolution 986 (1995), authorized States to permit the import of petroleum and petroleum products originating in Iraq, including financial and other essential transactions directly relating thereto, sufficient to produce a sum not

exceeding a total of $1 billion every 90 days. In paragraph 3 the Security Council stated that the resolution shall remain in force for 180 days.

(b) The authorization given by paragraph 2 of resolution 986 (1995) permitted Turkey to import petroleum and petroleum products originating in Iraq, sufficient to meet the pipeline tariff charges for the transport of these products through the Kirkuk-Yumurtalik pipeline in Turkey, after deduction of 30 per cent to the Compensation Fund. Resolution 1330 (2000) revised this deduction to 25 per cent. Due to the cessation of the "Oil-for-Food Programme" (the programme), pipeline tariff charges are no longer incurred.

(c) The provisions of resolution 986 (1995), which authorized sales of Iraqi oil not exceeding a total of $1 billion every 90 days, remained in force by resolutions 1111 (1997), 1129 (1997), 1143 (1997) and 1158 (1998) until 30 May 1998.

(d) The Security Council, in paragraphs 1 and 2 of resolution 1153 (1998), which took effect on 1 June 1998, decided that the authorization given to States by paragraph 1 of resolution 986 (1995) shall permit the import of petroleum and petroleum products originating in Iraq, including financial and other essential transactions directly relating thereto, sufficient to produce a sum not exceeding a total of $5.256 billion, in the 180-day mandate period referred to in paragraph 1 of resolution 1153 (1998). This provision of resolution 1153 (1998) remained in force by Council resolutions 1210 (1998), 1242 (1999) and 1284 (1999).

(e) By its resolution 1284 (1999) of 17 December 1999 the Security Council lifted the dollar cap and authorized sales of Iraqi oil of any volume during the 180-day mandate period. This resolution remained in force by Council resolutions 1302 (2000), 1330 (2000), 1352 (2001), which extended resolution 1330 (2000) for 30 days, 1360 (2001), 1382 (2001), 1409 (2002), 1443 (2002), which extended 1409 (2002) until 4 December 2002, and 1447 (2002), which extended the mandate to 3 June 2003. The final sale of oil under the programme was for shipments made on 20 March 2003.

(f) The Security Council, in paragraphs 1 and 3 of its resolution 1175 (1998), authorized States to permit the export to Iraq of the necessary parts and equipment ("spare parts") to enable Iraq to increase the export of petroleum and petroleum products, in quantities sufficient to produce the sum established in paragraph 2 of resolution 1153 (1998). The resolution stated that the funds in the escrow account pursuant to resolution 1153 (1998) up to $300 million may be used to meet any reasonable expenses, other than expenses payable in Iraq, which follow directly from contracts approved by the Committee established by resolution 661 (1990). Resolutions 1293 (2000) and 1302 (2000) established that up to $600 million may be authorized to permit States to export to Iraq the necessary parts and equipment to enable Iraq to increase the export of petroleum and petroleum products. Resolutions 1330 (2000), 1352 (2001), 1360 (2001), 1382 (2001), 1409 (2002) and 1447 (2002) retain the $600 million limit.

(g) Resolution 1330 (2000) allowed for funds up to $600 million from the escrow account to be used for the installation, maintenance, and training services of spare parts and equipment relating to the oil industry.

(h) The Security Council, in its resolution 1472 (2003), recognized that in view of the exceptional circumstances prevailing in Iraq, on an interim and

exceptional basis, technical and temporary adjustments should be made to the programme, and authorized the Secretary-General to make such changes for a period of 45 days.

(i) The Security Council, in its resolution 1476 (2003), decided that the provisions contained in paragraph 4 of resolution 1472 (2003) remain in force until 1 June 2003 and might be subject to further renewal by the Council.

(j) The Security Council, in its resolution 1483 (2003), requested the Secretary-General to terminate the programme within six months, and to transfer responsibility for the administration of any remaining activity to the Coalition Provisional Authority (the Authority). The Council also requested the consolidation of the accounts established pursuant to paragraphs 8 (a) "15 Governorates of Central and Southern Iraq" and 8 (b) "3 Governorates of Northern Iraq" of resolution 986 (1995).

(k) Sale of Iraqi oil is recognized as revenue in the fund for humanitarian activities in Iraq based on the bill of lading date and the total value of oil loaded as stipulated in the commercial invoice issued by the State Oil Marketing Organization. The proceeds from sale of Iraqi oil are allocated, upon receipt of deposits, to other accounts established pursuant to paragraph 8 of resolution 986 (1995). No oil sales were recorded after 20 March 2003.

(l) The funds from the sale of Iraqi oil pursuant to the authorization given by paragraph 1 of resolution 986 (1995) are to be used to meet the humanitarian needs of the Iraqi people and for the other purposes in paragraph 8 of resolution 986 (1995). In its resolution 1409 (2002), the Security Council permits the sale or supply of any commodities or products other than those referred to in paragraph 24 of resolution 687 (1991) as it relates to military commodities and products or military-related commodities, or products covered by the Goods Review List (S/2002/515) and its amendments as resolution 1454 (2002). The percentages used in allocating the oil sale proceeds were determined as follows:

(i) 53.034 per cent to finance the export to Iraq of medicine, health supplies, food and materials and supplies for essential civilian needs. Pursuant to resolution 1302 (2000) this was increased to 54.034 per cent and by resolution 1330 (2000) further increased to 59.034 per cent, less the payment referred to in paragraph (vi) below;

(ii) 13.0 per cent to complement the distribution by the Government of Iraq of goods imported by providing funds to the United Nations inter-agency humanitarian programme operating in the three northern governorates of Iraq, Arbil, Dihuok and Sulaimaniyeh;

(iii) 2.215 per cent to meet the operational and administrative costs of the United Nations;

(iv) 30.0 per cent allocated to the Compensation Fund established by the Security Council in its resolution 705 (1991). Pursuant to resolution 1330 (2000) this was decreased to 25.0 per cent;

(v) 0.751 per cent allocated to the United Nations Monitoring, Verification and Inspection Commission (UNMOVIC) established by the Security Council in its resolution 1284 (1999), which replaced the Special Commissions established by Security Council resolution 687 (1991) to meet operating costs.

(vi) A maximum of $10 million every 90 day period to be allocated to the escrow account established by the Security Council in its resolutions 706 (1991) and 712 (1991) for the payments envisaged under paragraph 6 of resolution 778 (1992). In resolution 1284 (1999) the Council suspended payments to this escrow account for an initial period of six months from 17 December 1999. In resolution 1302 (2000) the Council extended this suspension for a further 180-day period and transferred the allocation of (i) above. In resolution 1330 (2000) the Council reinstated the allocation of a maximum of $10 million every 90 days from 6 December 2000.

(m) Notwithstanding the periods for the sale of Iraqi oil as authorized by Security Council resolutions, financial statements I, II and III (United Nations Escrow Account) are prepared every six months.

(n) Included in financial statements I, II and III (United Nations Escrow Accounts) are details relating to the humanitarian activities, related operational and administrative costs, and pipeline tariff charges, that are undertaken under the provisions of Security Council resolution 986 (1995). From the beginning of the programme in December 1996 to mid-2000, implementation costs on actual expenditures incurred by agencies for activities associated with the purchase of humanitarian goods for northern Iraq were charged to the "Humanitarian activities in Iraq" account, and programme support costs on actual expenditures for the administrative and operational costs were charged to the "Administrative and operational costs" account. In mid-2000, following recommendations of the Board of Auditors, and taking into account the increased level of funds available in the "Administrative and operational costs" account, the Secretariat decided to prospectively charge all implementation and programme support costs to the "Administrative and operational costs" account. In mid-2002, the Secretariat reverted to the earlier treatment, whereby direct costs of implementing the programme in northern Iraq were charged to the "Humanitarian activities in Iraq" account. This decision reflected the need to harmonize treatment whether the work was done by the agency itself or contracted out. In 2003, when agencies began implementing various aspects of the programme in southern/central Iraq, these implementation costs were also charged to the "Humanitarian activities in Iraq" account, in line with the 2002 decision.

(o) The financial statements of the Compensation Fund, as referenced in paragraph (I) (iv) above, are reported on in a separate volume of the United Nations financial statements.

(p) Expenditure incurred during the biennium 2004-2005 for humanitarian supplies and spare parts relate to adjustments and reinstatements of contracts entered into in previous years.

Note 4
United Nations Escrow Account established under the provisions of Security Council resolutions 687 (1991), 706 (1991), 778 (1992) and 1284 (1999) (statements I, II and III)

(a) Included in financial statements I, II and III are the escrow accounts established by the Security Council in resolutions 706 (1991) and 712 (1991) for the payments envisaged under paragraph 6 of resolution 778 (1992), and the Special Account established by the Council in resolutions 687 (1991), 706 (1991) and

1284 (1999). These accounts were previously included in a separate volume. All comparative figures have been restated. The escrow account established under Security Council resolutions 706 (1991), 712 (1991) and 778 (1992) returned all funds in 2003. As a result, there are no further transactions to report relating to this escrow account.

(b) The escrow account administered by the Secretary-General under Security Council resolutions 706 (1991) and 712 (1991) provided for Iraqi funds from the sale of oil to be used for payment by the United Nations Compensation Commission, the full costs of carrying out the tasks authorized by section C of resolution 687 (1991), the full costs incurred by the United Nations in facilitating the return of all Kuwaiti property seized by Iraq, half the costs of the Boundary Commission, and the cost to the United Nations of implementing resolution 706 (1991), and of other necessary humanitarian activities in Iraq.

(i) With the refusal of Iraq to sell oil under the provisions of Security Council resolutions 706 (1991) and 712 (1991), the Security Council on 2 October 1992 adopted resolution 778 (1992) as an alternative means of providing funds for the purposes specified. Member States in which there were petroleum products owned by Iraq or Member States with funds of the Government of Iraq representing the proceeds of petroleum sales, paid for by the purchaser after 6 August 1990, were required to transfer some or all of these funds to the escrow account. Additionally, in resolution 778 (1992) the Council urged Member States to contribute funds from other sources to the escrow account. All such funds transferred or contributed to the escrow account under the provisions of resolution 778 (1992) were to be transferred back to the accounts of States from which funds were provided, together with applicable interest, at such time when oil exports have taken place pursuant to the system provided in resolutions 706 (1991) and 712 (1991) and the escrow account has received funds from the proceeds of sale. Iraqi oil exports began in December 1996 and in January 1997 the escrow account started receiving funds from the proceeds of sales that were transferred back to the accounts of States that provided the original funds to the escrow account.

(ii) In December 1999, pursuant to Security Council resolution 1284 (1999), payment to the escrow account from the proceeds of sales was suspended. The suspension, which was extended an additional 180 days by the Security Council in resolution 1302 (2000), was lifted by the Security Council in resolution 1330 (2000) in December 2000.

(iii) In May 2003 the Security Council in resolution 1483 (2003) requested the Secretary-General to restore funds that were provided by Member States pursuant to resolution 778 (1992). All such funds were returned in June 2003.

(c) The Security Council in resolution 687 (1991) requested the Secretary-General to undertake certain tasks in connection with the situation between Iraq and Kuwait. The costs of those activities were to be considered as an advance pending the receipt of payments to the Organization by Iraq in respect of certain activities, and by Iraq and Kuwait jointly in respect of the costs of the Boundary Commission.

(i) With the adoption by the Security Council of resolution 778 (1992), the above-mentioned costs have been covered by transfers from the escrow

account. Furthermore, the costs of the Special Commission are met by transfer from the escrow account pursuant to Security Council resolution 986 (1995);

(ii) The Security Council decided by resolution 1284 (1999) to establish the United Nations Monitoring, Verification and Inspection Commission (UNMOVIC). The responsibilities mandated to the Special Commission are undertaken by UNMOVIC;

(iii) The Security Council in resolutions 1483 (2003) and 1546 (2004) reaffirmed the Council's intention to revisit the mandate of UNMOVIC.

Note 5
Independent Inquiry Committee into the United Nations Oil-for-Food Programme expenditure

The Security Council in its resolution 1538 (2004) welcomed the Secretary-General's appointment of an independent high-level inquiry to investigate allegations concerning the United Nations Oil-for-Food Programme. Costs of the Committee are met from funds for administrative and operational costs of the programme. Expenditures during the biennium 2004-2005 ending 31 December 2005 were:

(Thousands of United States dollars)

Salaries	14 470.1
Consulting fees	15 277.6
Travel	3 225.6
Audit fees	98.4
Communication	280.0
Premises	1 182.1
Equipment	1 143.6
Miscellaneous supplies and services	176.5
Total	**35 853.9**

Note 6
Reimbursement of implementation costs by agencies

As a result of findings of the Independent Inquiry Committee into the United Nations Oil-for-Food Programme, some agencies were asked to return certain implementation costs paid to them in excess of their respective direct and indirect actual costs. As at 31 December 2005, $40,560,579 has been recorded in miscellaneous income under the "Humanitarian activities in Iraq" account, of which $40,342,668 had been received, and $217,911 was outstanding.

Note 7
Operating reserves

"Humanitarian activities in Iraq" account

An operating reserve of $159,971,000 was established during the six-month period ended 30 June 2005 under the "Humanitarian activities in Iraq" account. The reserve is to assure that sufficient funds are available for the satisfactory resolution of all remaining issues relating to outstanding letters of credit. With the reduction in outstanding letters of credit, the operating reserve was reduced to $126,660,000 as of 31 December 2005.

"Administrative and operational costs" account

An operating reserve of $48.0 million was established during the 12-month period ended 31 December 2004 under the "Administrative and operational costs" account. The reserve was to meet compensation costs payable in respect of those Oil-for-Food Programme staff members who were injured or killed as a result of the bombing of the United Nations headquarters building in Baghdad on 19 August 2003, as well as to set aside funds to meet the expected costs of the Independent Inquiry Committee and the administrative costs of the escrow accounts until all aspects of the programme are completed. During the period from 1 January 2005 to 31 December 2005, an amount of $37,242,808 was disbursed to meet these costs, including full settlement of all costs related to the Baghdad bombing of 19 August 2003. An additional reserve was established for $10,375,000, thereby resulting in an operating reserve of $21,132,192 as at 31 December 2005. This reserve is to meet future costs chargeable to the "Administrative and operational costs" account, including those relating to Independent Inquiry Committee and administrative costs.

Note 8
Non-expendable property

In accordance with United Nations accounting policies, non-expendable property is charged against the current allotment in the year of purchase. The non-expendable property valued at historical cost, according to the cumulative inventory records, is:

(Thousands of United States dollars)

	2005	2004
United Nations Office of the Humanitarian Coordinator for Iraq		3 082.4
UNMOVIC[a]	11 242.0	1 112.0
Agencies[a]	4 569.9	15 117.3
Office of the Iraq Programme		536.8
Independent Inquiry Committee	1 021.9	

[a] Due to the current situation in Iraq, it is not possible to fully ascertain the value of non-expendable property in Iraq as at 31 December 2005.

Note 9
Liabilities for end-of-service benefits

(a) Staff members who separate from the Organization are entitled to be paid for any unused vacation days they may have accrued up to a maximum of 60 days. The Organization's total liability for such unpaid accrued vacation compensation for staff working in the various activities related to Security Council resolutions 687 (1991), 706 (1991), 778 (1992), 986 (1995), 1284 (1999), and 1483 (2003) as of 31 December 2005 is estimated at $1.1 million.

(b) Some staff members are entitled to repatriation grant and related expenditures of relocation upon their separation from the Organization based on the number of years of service. The Organization's total liability for such unpaid repatriation and relocation entitlement for staff working in the various activities related to Security Council resolutions 687 (1991), 706 (1991), 778 (1992), 986 (1995), 1284 (1999), and 1483 (2003) as of 31 December 2005 is estimated at $0.9 million.

Note 10
Future modus operandi of United Nations Escrow Account established under Security Council resolution 986 (1995)

(a) The Security Council in resolution 1483 (2003) extended the Secretary-General's responsibilities under Council resolutions 1472 (2003) and 1476 (2003) for a period of six months. The Council requested the Secretary-General to terminate, in the most cost-effective manner, the ongoing operations of the programme at Headquarters and in the field by 21 November 2003, and to transfer responsibility for the administration of any remaining activity under the programme to the Authority.

(b) Accordingly, in the three Governorates of northern Iraq where the United Nations agencies were implementing the programme, contracts entered into by the agencies were transferred to the Authority. Similarly, in the 15 Governorates of central and southern Iraq, where, after the outbreak of hostilities agencies had been assigned responsibility for procurement activities previously undertaken by the Government of Iraq, uncompleted contracts were handed over to the Authority.

(c) The Security Council in resolution 1546 (2004) decided that in connection with the dissolution of the Authority, the Interim Government of Iraq and its successors shall assume the rights, responsibilities and obligations relating to the programme that were transferred to the Authority, including all operational responsibility for the programme and any obligations undertaken by the Authority in connection with such responsibility, and responsibility for ensuring independently authenticated confirmation that goods have been delivered, and further decided that following a 120-day transition period from the date of adoption of the resolution, the Interim Government of Iraq and its successors shall assume all responsibility for certifying delivery of goods under previously prioritized contracts, and that such certification shall be deemed to constitute the independent authentication required for the release of funds associated with such contracts, consulting as appropriate to ensure the smooth implementation of those arrangements.

(d) As of 31 December 2005, the liquidation of the programme continued. All obligations relating to contracts that had not been prioritized in accordance with

Security Council resolution 1483 (2003) were closed, except for those where letters of credit had not lapsed. Obligations relating to contracts that had been prioritized remain as liabilities of the programme, and the related letters of credit have not been closed. The expiry dates for the letters of credit extend until 2007. In his letters dated 8 August 2005, 17 October 2005 and 19 December 2005, the Secretary-General kept the Security Council informed of the arrangements for the liquidation of the outstanding letters of credit, and of the progress being made. The Security Council has taken note of the matter.

(e) Since the adoption of Security Council resolution 1483 (2003), a total amount of $10.040 billion has been transferred to the Development Fund for Iraq up to 31 December 2005, with $4.440 billion being transferred during the biennium 2004-2005. The remaining surplus funds will be returned to the Development Fund for Iraq in accordance with the provisions of paragraph 17 of Security Council resolution 1483 (2003).

Note 11
Contingent liabilities

In accordance with Security Council resolution 1483 (2003), as part of the liquidation process, all claims and disputes involving the United Nations or its agencies with third parties, in carrying out the activities of the programme are to be transferred to, and become the responsibility of, the Authority. There may be some circumstances in which such a transfer is not possible and any liability and related fees will need to be met by the programme. The amount is estimated at $5 million.

Note 12
Investigation by the Independent Inquiry Committee

In April 2004, the Secretary-General appointed a high-level, Independent Inquiry Committee to investigate the administration and management of the Oil-for-Food Programme from its inception to its transfer to the Coalition Provincial Authority, including allegations of fraud and corruption on the part of United Nations officials, personnel and agents as well as contractors, including entities that have entered into contracts with the United Nations or with Iraq under the programme. Following this, the Security Council adopted resolution 1538 (2004), in which it welcomed the inquiry. The Committee completed its investigation and issued its final report on 27 October 2005.

The Committee recognized that the programme was unique to the United Nations in many aspects, namely its sheer size, scope and political and geographic complexities. The Committee concluded that, inter alia, the former Government of Iraq had manipulated the programme to dispense contracts on the basis of political preference and to derive illicit payments from companies; that there were shortcomings in the United Nations procurement, management and programme implementation areas; that audit and oversight mechanisms in the United Nations needed to be strengthened; and that the former Executive Director of the programme "corruptly benefited" from it. On the other hand, the Committee had positive findings relating to controls and procedures applied with respect to the account for "Administrative and operational costs" and treasury operations.

The Committee made recommendations related to the United Nations and to the programme, and the Secretariat is taking appropriate action accordingly.